

## **EXECUTIVE SUMMARY**

### **The Statewide Single Audit of the Commonwealth of Kentucky For the Year Ended June 30, 2003**

## **BACKGROUND**

The Single Audit Act of 1984, subsequent amendments, and corresponding regulations, require the auditing of financial statements and the compliance and internal controls applicable to federal moneys received by the Commonwealth.

## **STATE AGENCIES EXPENDED MORE FEDERAL AWARDS IN FY 03**

Total federal expenditures increased by \$322,754,968 in FY 03. State organizations expended \$6,524,318,277 in federal awards in FY 03; whereas, state organizations expended \$6,201,563,309 in federal awards in FY 02.

## **FEWER FINDINGS IN FY 03**

There were 11 fewer findings in FY 03, than in FY 02. There were 41 findings for FY 03; whereas there were 53 findings in FY 02.

## **STATE AGENCIES WITH RESOLVED PRIOR AUDIT FINDINGS AND NO NEW FINDINGS IN FY 03**

Kentucky Access Program  
Personnel Cabinet  
Council on Postsecondary Education  
State Treasurer

## **STATE AGENCIES WITH RECURRING FINDINGS**

### **Cabinet for Families and Children**

- Password Security
- Subrecipient Monitoring
- Eligibility Requirements for Benefits
- Support for Expenditures

### **Finance and Administration Cabinet**

- Classification and Categorization of Investments in the Cash and Investments Note for CAFR
- Procedures for the Cash and Investment Statistical Analysis System Programs
- Segregation of Duties, Office of Financial Management
- Necessity of User Accounts

**The Statewide Single Audit of the Commonwealth of Kentucky  
For the Year Ended June 30, 2003  
(Continued)**

**STATE AGENCIES WITH RECURRING FINDINGS (Continued)**

Cabinet for Health Services

- Asset Security and Segregation of Duties, Vital Statistics Branch
- Identity Theft Risks, Vital Statistics Branch

Justice Cabinet

- Indirect Cost Plan Submission to Cognizant Federal Agency
- Subrecipient Monitoring
- Quarterly Status Report and Supporting Documentation

Department of Military Affairs

- Subrecipient Monitoring

Revenue Cabinet

- Maintenance of Tax Files
- Automation Process for Accelerated Tax Returns
- Security for Administrator Accounts
- Necessity of User Accounts

Transportation Cabinet

- Procedures to Ensure Accurate Presentation of Federal Highway Administration Statistics Report
- Federal Guideline Compliance for the Federal Highway Administration Statistics Report
- Federal Highway Administration Approvals Prior to Advertising for Projects

Cabinet for Workforce Development

- Security for Administrator Accounts
- Subrecipient Monitoring and Follow Up, Department for Training and ReEmployment
- Local Area Network Server Security
- Adequate Maintenance of Employer Accounts, Division of Unemployment Insurance

**STATE AGENCIES WITH UNRESOLVED  
FEDERAL AWARD QUESTIONED COSTS IN FY 03**

Cabinet for Families and Children	\$14,667 (FY 03)
Cabinet for Families and Children	\$ 2,616 (FY 02)
Justice Cabinet	\$46,774 (FY 03)



CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS

March 26, 2004

To the People of Kentucky  
Honorable Ernie Fletcher, Governor  
Cabinet Secretaries and Agency Heads  
Members of the Commonwealth of Kentucky Legislature

As Auditor of Public Accounts, I am pleased to transmit herewith our report of the Statewide Single Audit of the Commonwealth of Kentucky for the year ended June 30, 2003. The Federal Government's Office of Management and Budget (OMB), per OMB Circular A-133 requires the Auditor of Public Accounts to perform the Statewide Single Audit of the Commonwealth of Kentucky.

To fulfill these requirements, the Auditor of Public Accounts, performs the following:

- An audit of the basic financial statements and combining and individual fund statements and schedules-nonmajor funds;
- Limited procedures applied to required supplementary information;
- An audit of the Schedule of Expenditures of Federal Awards;
- An audit of compliance with the compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each major federal program;
- Tests of internal control over compliance in accordance with OMB Circular A-133;
- Tests of compliance with certain provisions of laws, regulations, contracts, and grants; and
- Tests of internal control over financial reporting.

The Auditor of Public Accounts also calculates a dollar threshold, based on OMB Circular A-133 guidance, to determine the federal programs to be audited for internal controls and compliance. For FY 03, the threshold for auditing federal programs was \$18 million.

To the People of Kentucky  
Honorable Ernie Fletcher, Governor  
Cabinet Secretaries and Agency Heads  
Members of the Commonwealth of Kentucky Legislature

In FY 03, the following state agencies had prior audit findings resolved and no new findings: Kentucky Access Program, Personnel Cabinet, Council on Postsecondary Education, and Office of the State Treasurer.

On behalf of the Division of Financial Audit of the Auditor of Public Account's Office, I wish to thank the employees of the Commonwealth for their cooperation during the course of our audit. Should you have any questions concerning this report, please contact Charlene Daniels, CPA, Acting Director, Division of Financial Audit, or me.

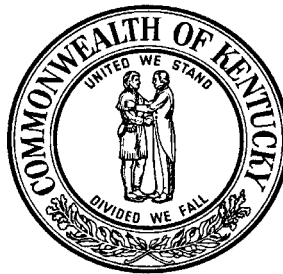
Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen  
Auditor of Public Accounts

**REPORT OF THE STATEWIDE SINGLE AUDIT  
OF THE  
COMMONWEALTH OF KENTUCKY**

**For the Year Ended June 30, 2003**



**CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS  
[www.kyauditor.net](http://www.kyauditor.net)**

**105 SEA HERO ROAD, SUITE 2  
FRANKFORT, KY 40601  
TELEPHONE (502) 573-0050  
FACSIMILE (502) 573-0067**



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## **INTRODUCTION**

**COMMONWEALTH OF KENTUCKY  
INTRODUCTION  
FOR THE YEAR ENDED JUNE 30, 2003**

Single Audit Report

The Auditor of Public Accounts (APA), acting as principal auditor in conjunction with various certified public accounting firms, annually performs a statewide single audit of the Commonwealth of Kentucky.

The APA prepares the Single Audit Report in compliance with Government Auditing Standards, Generally Accepted Government Auditing Standards, and the requirements of Office of Management and Budget (OMB) Circular A-133. The APA, on behalf of the Commonwealth of Kentucky, also prepares a reporting package as required by OMB Circular A-133. The reporting package includes the basic financial statements, Schedule of Expenditures of Federal Awards (SEFA), auditor's reports, Summary Schedule of Prior Audit Findings, and corrective action plans. For the fiscal year ended June 30, 2003 (FY 03), the Single Audit Report is presented in two reports: the Comprehensive Annual Financial Report (CAFR) and the Single Audit Report.

The CAFR, which contains the basic financial statements and the auditor's report thereon, has been issued under separate cover.

The Single Audit Report contains the auditor's reports on compliance and internal control over financial reporting, compliance and internal control over compliance with requirements applicable to major federal programs, and the supplementary SEFA. The Single Audit Report also contains the SEFA, Schedule of Findings and Questioned Costs, and the Summary Schedule of Prior Audit Findings.

Schedule of Expenditures of Federal Awards

The SEFA is organized by federal grantor. The Catalog of Federal Domestic Assistance (CFDA) numbers and program names are listed under the federal grantor administering the program. The state organizations expending the federal funds are listed beside each CFDA number. The notes to the SEFA provide more detailed information on certain aspects of the expenditures. Clusters of programs are indicated in the schedule by light gray shading.

Schedule of Findings and Questioned Costs

The Schedule of Findings and Questioned Costs consists of three (3) sections: Summary of Auditor's Results, Financial Statement Findings, and Federal Award Findings and Questioned Costs. The Summary of Auditor's Results summarizes the type of audit reports issued and lists major programs audited. The Financial Statement Findings list the audit findings related to the financial statements. The Federal Award Findings and Questioned Costs lists all findings related to federal awards. In both sections, reportable conditions and reportable instances of noncompliance are presented first, then material weaknesses and material instances of noncompliance.

**COMMONWEALTH OF KENTUCKY  
INTRODUCTION  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

Summary Schedule of Prior Audit Findings

Audit findings reported in the Schedule of Findings and Questioned Costs for FY 02, as well as any previous findings that have not been resolved, are reported in the Summary Schedule of Prior Audit Findings for FY 03.

The Summary Schedule of Prior Audit Findings is organized based on whether the prior year finding was reportable or material. The findings of each classification (reportable and material) are categorized as (1) fully corrected, (2) not corrected or partially corrected, (3) corrective action taken differs significantly from corrective action previously reported, or (4) finding no longer valid or does not warrant further action.

Audit Approach

The scope of the statewide single audit for FY 03 included:

- An audit of the basic financial statements and combining and individual fund statements and schedules-nonmajor funds;
- Limited procedures applied to required supplementary information;
- An audit of the SEFA;
- An audit of compliance with the compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each major federal program;
- Tests of internal control over compliance in accordance with OMB Circular A-133;
- Tests of compliance with certain provisions of laws, regulations, contracts, and grants; and
- Tests of internal control over financial reporting.

Status of State Universities

The Single Audit Act Amendments permit the single audit to cover the entire operations of the entity or include a series of audits covering departments, agencies, or other organizational units expending federal awards. The agencies audited as part of the Statewide Single Audit of the Commonwealth of Kentucky are listed in Appendix 1. The Commonwealth has elected to exclude state universities from the statewide single audit, except as part of the audit of the general-purpose financial statements. Thus, state universities are not included in the accompanying Schedule of Expenditures of Federal Awards and reports on internal control and compliance. It should be noted, however, that state universities are still required to have audits performed in accordance with the provisions of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

**COMMONWEALTH OF KENTUCKY  
INTRODUCTION  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report

ABC	Department of Alcoholic Beverage Control
ADD	Area Development District
AGR	Department of Agriculture
AOC	Administrative Office of the Courts
APA	Auditor of Public Accounts
ASL	Agency Security Lead
BDC	Backup Domain Controllers
BMS	Bridge Management System
CAFR	Comprehensive Annual Financial Report
CAMRA	Complete Asset Management Reporting and Accounting System
CAP	Cost Allocation Plan
CCDBG	Child Care and Development Block Grant
CCSHCN	Commission for Children with Special Health Care Needs
CD	Compact Disk
CFC	Cabinet for Families and Children
CFDA	Catalog of Federal Domestic Assistance
CFR	Code of Federal Regulations
CHFS	Cabinet for Health and Family Services
CHS	Cabinet for Health Services
CMB	Contracts Management Branch
CORR	Department of Corrections
CPA	Certified Public Accountant
CPE	Council on Postsecondary Education
CSE	Child Support Enforcement
CVC	Crime Victims Compensation Board
CWD	Cabinet for Workforce Development
DBA	Database Administrator
DCD	Department for Community Development
DCJT	Department of Criminal Justice Training
DFS	Division of Family Support
DHHS	United States Department of Health and Human Services
DLA	Department for Libraries and Archives
DLG	Department for Local Government
DLN	Document Locator Number
DMA	Department of Military Affairs
DOB	Date of Birth
DOL	Department of Labor
DOT	Department of Transportation



**COMMONWEALTH OF KENTUCKY  
INTRODUCTION  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report (Continued)

DPH	Department for Public Health
DTR	Department for Training and ReEmployment
DVD	Digital Versatile Disc
EDU	Department of Education
EMSB	Emergency Medical Services Board
EPA	Unites States Environmental Protection Agency
EPSB	Education Professional Standards Board
ERA	Employment Retention Assistance
F&W	Department of Fish and Wildlife Resources
FBI	Federal Bureau of Investigations
FAC	Finance and Administration Cabinet
FAP	Finance and Administration Policies
FHWA	Federal Highway Administration
Finance	Finance and Administration Cabinet
FTP	File Transfer Protocol
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GASB	Governmental Accounting Standards Board
GMB	Grants Management Branch
GOT	Governor's Office for Technology
GOV	Office of the Governor
GUI	Graphical User Interface
HIS	Highway Information System
HRC	Kentucky Commission on Human Rights
ID	Identification
IDCRP	Indirect Cost Rate Proposal
INQR	Inquiry
IRC	Internet Relay Chat
IRS	Internal Revenue Service
JGTRRA	Jobs and Growth Tax Relief Reconciliation Act
JTPA	Job Training Partnership Act
JUST	Justice Cabinet, Office of the Secretary
JUV	Department of Juvenile Justice
KAC	Kentucky Arts Council
KAMES	Kentucky Automated Management and Eligibility System
KAP	Kentucky Access Program
KBIS	Kentucky Bridge Information System
KCA	Kentucky Center for the Arts
KDE	Kentucky Department of Education

**COMMONWEALTH OF KENTUCKY  
INTRODUCTION  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report (Continued)

KEIN	Kentucky Employer Identification Number
KET	Kentucky Educational Television
KEWS	Kentucky Electronic Workplace for Employment Services
KHCORP	Kentucky Housing Corporation
KHCOUN	Kentucky Heritage Council
KHEAA	Kentucky Higher Education Assistance Authority
KHESLC	Kentucky Higher Education Student Loan Corporation
KHS	Kentucky Historical Society
KIA	Kentucky Infrastructure Authority
KRC	Kentucky Revenue Cabinet
KRS	Kentucky Revised Statutes
KSP	Kentucky State Police
KST	Office of the Kentucky State Treasurer
K-TAP	Kentucky Transitional Assistance Program
KWP	Kentucky Works Program
KY	Kentucky
KyEM	Kentucky Division of Emergency Management
LAB	Labor Cabinet
M&M	Mines and Minerals
MARS	Management Administrative and Reporting System
MFE	Modernized Front End
MIL	Department of Military Affairs
MMTASK	Multimedia Support Task
MRDB	Management Reporting Database
NA	Not Applicable
NBIS	National Bridge Information System
NREPC	Natural Resources and Environmental Protection Cabinet
NT	New Technology
OAG	Office of the Attorney General
OFM	Office of Financial Management
OIG	Office of Inspector General
OMB	Office of Management and Budget
OMS	Operations Management System
PA	Public Assistance
PARKS	Department of Parks
PC	Personal Computer
PCR	Program Change Request
PDC	Primary Domain Controller
PMS	Pavement Management System
PSC	Public Service Commission

**COMMONWEALTH OF KENTUCKY  
INTRODUCTION  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report (Continued)

PUBAD	Department of Public Advocacy
R&D	Research and Development
RDS	Remote Document Security
REV	Kentucky Revenue Cabinet
Revenue	Kentucky Revenue Cabinet
RHP	Replacement Housing Payments
RMDS	Report and Management Distribution System
SAS	Statistical Analysis System
SBE	State Board of Elections
SDLC	System Development Life Cycle
SEFA	Schedule of Expenditures of Federal Awards
SF	Short Form
SFAG	State Family Assistance Grant
SLA	Service Level Agreement
SMTP	Simple Mail Transfer Protocol
SQL	Structured Query Language
SSWAK	Statewide Single Audit of the Commonwealth of Kentucky
SYS	Oracle System Administrator Account
TANF	Temporary Assistance for Needy Families
TC	Transportation Cabinet
TRAV	Department of Travel
UI	Unemployment Insurance
UK	University of Kentucky
UPS	Unified Prosecutorial System
U.S.	United States
USC	United States Code
USDA	United States Department of Agriculture
VA	Department of Veterans' Affairs
VAWA	Violence Against Women Formula Grants
VNC	Virtual Network Client
VOCA	Crime Victim Assistance Grant
WebDB	Web Database
WIA	Workforce Investment Act
WtW	Welfare-to-Work

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of Agriculture					
Direct Programs:					
10.025	Plant and Animal Disease, Pest Control, and Animal Care	AGR	\$ 198,718	\$	\$
10.028	Wildlife Services (Note 9)	F&W	17,988		
10.064	Forestry Incentives Program (Note 14)	NREPC			
10.069	Conservation Reserve Program (Note 14)	NREPC	31,113		
		F&W			
10.153	Market News (Note 14)	AGR			
10.163	Market Protection and Promotion	AGR	72,393		
10.164	Wholesale Market Development	AGR	54,900		
10.167	Transportation Services	AGR	22,000		
10.550	Food Donation (Note 13)	AGR		13,474,504	
Food Stamp Cluster:					
10.551	Food Stamps (Note 2) (Note 13)	CFC		467,646,178	
10.561	State Administrative Matching Grants for Food Stamp Program (Note 2)	CFC	25,581,061		488,916
		OAG	369,770		
		CHS	155,835		
Child Nutrition Cluster:					
10.553	School Breakfast Program (Note 2)	EDU	31,105,721		31,020,020
		JUV	336,379		
10.555	National School Lunch Program (Note 2)	EDU	96,325,008		96,156,294
		JUV	540,648		
10.556	Special Milk Program for Children (Note 2)	EDU	93,914		93,914
10.559	Summer Food Service Program for Children (Note 2)	EDU	4,532,272		4,393,458
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children (Note 2)	CHS	80,187,442		14,794,805
10.558	Child and Adult Care Food Program (Note 2)	EDU	25,044,722		24,658,415
10.560	State Administrative Expenses for Child Nutrition	EDU	1,756,228		
		AGR	130,557		
10.565	Commodity Supplemental Food Program (Note 4) (Note 13)	AGR	400,146	1,395,394	
Emergency Food Assistance Cluster:					
10.568	Emergency Food Assistance Program (Administrative Costs)	AGR	1,532,006		
10.569	Emergency Food Assistance Program (Food Commodities) (Note 13)	AGR		6,753,576	
10.570	Nutrition Services Incentive	CHS	1,226,231		1,226,230
10.572	WIC Farmers' Market Nutrition Program (FMNP)	AGR	133,267		
10.652	Forestry Research	NREPC	115,277		
10.664	Cooperative Forestry Assistance (Note 13)	NREPC	2,490,980	327,265	425,055
10.672	Rural Development, Forestry, and Communities	NREPC	94,493		65,370
10.766	Community Facilities Loans and Grants (Note 2) (Note 3e) (Note 13)	KHCORP		67,738,386	

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<b><u>U.S. Department of Agriculture (Continued)</u></b>					
<b>Direct Programs (Continued):</b>					
10.769	Rural Business Enterprise Grants (Note 14)	AGR			
10.771	Rural Cooperative Development Grants (Note 14)	AGR			
10.912	Environmental Quality Incentives Program	NREPC	503		
10.914	Wildlife Habitat Incentive Program (Note 13)	F&W	60,103	15,750	
NA	Rural Rehabilitation Student Loan Program (Note 3a)	AGR	114,232		
<b>Total U.S. Department of Agriculture</b>			<b>\$ 272,723,907</b>	<b>\$ 557,351,053</b>	<b>\$ 173,322,477</b>
<b><u>U.S. Department of Commerce</u></b>					
<b>Direct Programs:</b>					
11.305	Economic Development - State and Local Economic Development Planning	DLG	\$ 106,402		\$ 62,290
<b><u>Public Works and Economic Development Cluster:</u></b>					
11.307	Economic Adjustment Assistance (Note 3b)	DLG	41		
11.450	Integrated Flood Observing and Warning System (IFLOWS)	MIL	51,470		
11.550	Public Telecommunications Facilities-Planning and Construction (Note 2)	KET	462,090		
<b><u>Passed Through From Personal Responsibility in A Desirable Environment:</u></b>					
11.469	Congressionally Identified Construction Projects Pass Through Grantor's #-NA	NREPC	292,853		
<b>Total U.S. Department of Commerce</b>			<b>\$ 912,856</b>		<b>\$ 62,290</b>
<b><u>U.S. Department of Defense</u></b>					
<b>Direct Programs:</b>					
12.002	Procurement Technical Assistance For Business Firms	DCD	\$ 156,910		\$
12.113	State Memorandum of Agreement Program for the Reimbursement of Technical Services	NREPC	400,390		
12.400	Military Construction, National Guard	MIL	518,751		
12.401	National Guard Military Operations and Maintenance (O & M) Projects	MIL	11,968,283		
12.404	National Guard Civilian Youth Opportunities	MIL	1,500,044		
NA	Chemical Demilitarization and Remediation Activity for Hazardous Waste Activities at Chemical Demilitarization Facilities	NREPC	55,451		12,109
NA	Helicopter Repair Hangar, Bluegrass Station	MIL	266,248		
NA	Teacher and Teacher's Aide Placement Assistance Program	EPSB	89,679		
NA	Metal Office Building, Bluegrass Station	MIL	44,812		
NA	Monitoring of Wildlife	F&W	24,826		
<b>Total U.S. Department of Defense</b>			<b>\$ 15,025,394</b>		<b>\$ 12,109</b>

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2003**  
**(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of Housing and Urban Development					
Direct Programs:					
14.117	Mortgage Insurance - Homes (Note 2) (Note 3e) (Note 13)	KHCORP	\$	\$ 128,206,362	\$
14.169	Housing Counseling Assistance Program	KHCORP		97,826	
Section 8 Project-Based Cluster:					
14.182	Lower Income Housing Assistance Program-Section 8 New Construction/Substantial Rehabilitation (Note 2)	KHCORP		84,569,085	
14.856	Lower Income Housing Assistance Program-Section 8 Moderate Rehabilitation (Note 2)	KHCORP		240,015	
14.228	Community Development Block Grants/State's Program (Note 2) (Note 10)	DLG		31,637,089	30,783,802
		HRC		24,666	
14.231	Emergency Shelter Grants Program	KHCORP		1,296,046	1,257,032
14.235	Supportive Housing Program (Note 2)	KHCORP		3,245,684	3,216,564
14.238	Shelter Plus Care	KHCORP		255,447	106,705
14.239	HOME Investment Partnerships Program (Note 2)	KHCORP		17,182,667	10,021,463
14.241	Housing Opportunities for Persons with AIDS	KHCORP		891,415	867,997
14.401	Fair Housing Assistance Program-State and Local	HRC		185,817	
14.408	Fair Housing Initiatives Program	HRC		1,463	
14.409	Fair Housing Initiatives Program (FHIP) Education and Outreach Initiative	HRC		70,458	
14.871	Section 8 Housing Choice Vouchers (Note 2)	KHCORP		20,485,291	
NA	HUD Disaster Recovery Initiative	DLG		297,079	297,079
Total U.S. Department of Housing and Urban Development			\$	160,480,048	\$ 128,206,362 \$ 46,550,642
U.S. Department of the Interior					
Direct Programs:					
15.250	Regulation of Surface Coal Mining and Surface Effects of Underground Coal Mining	NREPC	\$	13,171,452	\$
15.252	Abandoned Mine Land Reclamation (AMLR) Program (Note 2) (Note 13)	NREPC		16,168,161	50,372 5,198,054
Fish and Wildlife Cluster:					
15.605	Sport Fish Restoration (Note 9)	F&W		3,926,878	
15.611	Wildlife Restoration (Note 11)	F&W		3,310,425	
15.608	Fish and Wildlife Management Assistance	NREPC		16,284	
15.615	Cooperative Endangered Species Conservation Fund (Note 9)	F&W		207,149	
		NREPC		39,056	563
15.616	Clean Vessel Act	F&W		31,362	
15.617	Wildlife Conservation and Appreciation (Note 14)	F&W			
15.618	Administrative Grants for Federal Aid in Sport Fish and Wildlife Restoration	F&W		610	

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of the Interior (Continued)					
Direct Programs (Continued):					
15.622	Sportfishing and Boating Safety Act	F&W	200,000		
15.623	North American Wetlands Conservation Fund (Note 14)	NREPC	40,000		
		F&W			
15.625	Wildlife Conservation and Restoration (Note 9)	F&W	217,896		
15.634	State Wildlife Grants (Note 9)	F&W	666,588		
15.808	U.S. Geological Survey-Research and Data Acquisition (Note 13) (Note 14)	NREPC		58,500	
		F&W			
15.810	National Cooperative Geologic Mapping Program (Note 14)	F&W			
15.904	Historic Preservation Fund Grants-In-Aid	KHCOUN	655,583		179,728
15.916	Outdoor Recreation-Acquisition, Development and Planning (Note 7) (Note 14)	DLG	940,674		940,674
		PARKS			
NA	Wolf Creek National Fish Hatchery (Note 14)	F&W			
NA	National Fish and Wildlife Foundation-Restoration of Elk Habitat in Kentucky	F&W	14,255		
Total U.S. Department of the Interior			\$ 39,606,373	\$ 108,872	\$ 6,319,019
U.S. Department of Justice					
Direct Programs:					
16.007	State Domestic Preparedness Equipment Support Program	MIL	\$ 1,592,106		\$
		AGR	8,726		
16.523	Juvenile Accountability Incentive Block Grants	JUV	2,475,389		415,832
		AOC	70,380		
		PUBAD	61,601		
		UPS	26,945		
16.540	Juvenile Justice and Delinquency Prevention-Allocation to States	JUV	1,382,606		1,258,001
16.541	Juvenile Justice and Delinquency Prevention-Special Emphasis	AOC	29,435		
16.543	Missing Children's Assistance	KSP	6,559		
16.548	Title V-Delinquency Prevention Program	JUV	330,942		297,461
16.549	Part E-State Challenge Activities	JUV	96,567		96,567
16.550	State Justice Statistics Program for Statistical Analysis Centers	JUST	75,002		
16.554	National Criminal History Improvement Program (NCHIP) (Note 14)	KSP	45,772		
		JUST			
16.560	National Institute of Justice Research, Evaluation, and Development Project Grants	JUST	13,800		
16.564	Crime Laboratory Improvement-Combined Offender DNA Index System Backlog Reduction	KSP	534		
16.575	Crime Victim Assistance	JUST	4,773,634		4,648,826
		UPS	537,574		
16.576	Crime Victim Compensation	CVC	21,470		

See accompanying Notes to the Schedule of Expenditures of Federal Awards



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State	Expenditures		Provided to Subrecipient
		Organizations	Cash	Noncash	
U.S. Department of Justice (Continued)					
Direct Programs (Continued):					
16.579	Byrne Formula Grant Program	JUST	4,100,446		4,031,874
		KSP	2,074,156		
		AOC	904,335		54,623
		PUBAD	122,606		
		OAG	86,858		72,164
		JUV	59,333		59,333
		UPS	22,240		
		CORR	10,988		
16.580	Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program (Note 14)	JUST	1,185,963		
		AOC	1,042,435		
		UPS	232,965		
		DCJT	9,583		
		CFC			
16.585	Drug Court Discretionary Grant Program (Note 9)	AOC	813,614		
16.586	Violent Offender Incarceration and Truth in Sentencing Incentive Grants	CORR	3,284,798		
		JUST	16,075		
		JUV	1,830		
16.588	Violence Against Women Formula Grants	JUST	1,528,921		1,450,395
		UPS	200,664		
		OAG	68,085		
		GOV	66,172		
		AOC	24,534		
16.589	Rural Domestic Violence and Child Victimization Enforcement Grant Program	JUST	139,065		139,065
16.592	Local Law Enforcement Block Grants Program	KSP	463,571		
		JUST	411,412		371,949
		AOC	22,286		
		PARKS	13,625		
16.593	Residential Substance Abuse Treatment for State Prisoners (Note 14)	CORR	943,249		
		JUST			
16.607	Bulletproof Vest Partnership Program (Note 14)	JUST			
		KSP			
		F&W			
16.609	Community Prosecution and Project Safe Neighborhoods	UPS	118,495		
16.710	Public Safety Partnership and Community Policing Grants (Note 14)	KSP	1,442,973		
		CORR	21,492		
		JUST			
16.712	Police Corps	DCJT	2,008,915		
16.727	Enforcing Underage Drinking Laws Program	KSP	243,067		181,811
		ABC	149,653		
16.728	Drug Prevention Program	TC	29,383		
NA	Drug Enforcement Administration	KSP	691,899		
NA	Federal Bureau of Investigation	KSP	14,326		
NA	Federal Methamphetamine Initiative	KSP	67,541		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of Justice (Continued)					
Passed Through From Eastern Kentucky University:					
16.710	Public Safety Partnership and Community Policing Grants Pass Through Grantor's #-97-CK-WK-1 (Note 14)	DCJT			
Total U.S. Department of Justice			\$ 34,186,595		\$ 13,077,901
U.S. Department of Labor					
Direct Programs:					
17.002	Labor Force Statistics	CWD	\$ 1,038,743		\$
17.005	Compensation and Working Conditions	LAB	144,663		
17.203	Labor Certification for Alien Workers	CWD	301,942		
Employment Services Cluster:					
17.207	Employment Service	CWD	12,272,201		5,994
17.801	Disabled Veterans' Outreach Program (DVOP)	CWD	709,459		
17.804	Local Veterans' Employment Representative Program	CWD	747,955		
17.225	Unemployment Insurance (Note 2) (Note 5)	CWD	640,076,477		5,987
17.235	Senior Community Service Employment Program	CHS	1,656,901		1,623,913
17.245	Trade Adjustment Assistance-Workers (Note 2)	CWD	18,516,129		
17.253	Welfare-to-Work Grants to States and Localities (Note 14)	CFC	672,843		674,021
		CHS			
17.255	Workforce Investment Act (Note 2) (Note 12)	CWD	109,196		95,546
Workforce Investment Act Cluster:					
17.258	WIA Adult Program (Note 2)	CWD	13,537,375		13,414,127
17.259	WIA Youth Activities (Note 2)	CWD	14,264,083		13,273,095
		EDU	946,703		831,246
17.260	WIA Dislocated Workers (Note 2) (Note 12)	CWD	19,565,986		18,111,151
17.263	Youth Opportunity Grants	CWD	47,112		24,923
17.267	WIA Incentive Grants-Section 503 Grants to States	CWD	1,410,281		800,407
		MIL	176,581		
17.503	Occupational Safety and Health-State Program	LAB	3,151,226		
17.504	Consultation Agreements	LAB	13,762		
17.600	Mine Health and Safety Grants	M&M	598,500		
Total U.S. Department of Labor			\$ 729,958,118		\$ 48,860,410
U.S. Department of Transportation					
Direct Programs:					
20.005	Boating Safety Financial Assistance	F&W	\$ 454,551		\$
20.106	Airport Improvement Program	TC	18,377		
		MIL	19,205		

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**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of Transportation (Continued)					
Direct Programs (Continued):					
Highway Planning and Construction Cluster:					
20.205	Highway Planning and Construction (Note 2) (Note 6) (Note 15)	TC	485,248,638		
		KSP	290		
20.218	National Motor Carrier Safety	TC	3,934,453		94,459
		KSP	202,328		
20.219	Recreational Trails Program (Note 7)	DLG	589,467		535,427
		PARKS	6,813		
20.505	Federal Transit-Metropolitan Planning Grants	TC	474,183		460,091
Federal Transit Cluster:					
20.507	Federal Transit-Formula Grants	TC	10,791,834		10,791,834
20.509	Formula Grants for Other Than Urbanized Areas	TC	6,387,911		6,023,219
20.513	Capital Assistance Program for Elderly Persons and Persons with Disabilities	TC	1,777,557		1,727,806
Highway Safety Cluster:					
20.600	State and Community Highway Safety (Note 14)	KSP	4,709,848		1,460,690
		CHS	9,091		9,091
		DCJT			
		TC			
20.604	Safety Incentive Grants for Use of Seatbelts	KSP	499,173		345,160
20.605	Safety Incentives to Prevent Operation of Motor Vehicles by Intoxicated Persons	KSP	929,242		
20.700	Pipeline Safety	PSC	259,800		
20.703	Interagency Hazardous Materials Public Sector Training and Planning Grants	MIL	157,791		
Total U.S. Department of Transportation			\$ 516,470,552		\$ 21,447,777
U.S. Department of Treasury					
21.999	Job Growth Tax Relief Reconciliation Act (Note 2)	FAC	\$ 68,720,606		
NA	Internal Revenue Service (Note 14)	KSP			
Total U.S. Department of Treasury			\$ 68,720,606		
U.S. Appalachian Regional Commission					
Direct Programs:					
23.001	Appalachian Regional Development	DLG	\$ 84,551		\$ 433,329
23.002	Appalachian Area Development	DLG	433,329		433,329

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<b><u>U.S. Appalachian Regional Commission (Continued)</u></b>					
<b>Direct Programs (Continued):</b>					
23.005	Appalachian Housing Project Planning Loan, Technical Assistance Grant and Site Development and Off-Site Improvement Grant-State Appalachian Housing Programs (Note 14)	KHCORP	1,220,748		
23.011	Appalachian State Research, Technical Assistance, and Demonstration Projects	DLG	105,065		149,179
		FAC	38,653		38,653
NA	Kentucky Appalachian Motorcoach Tourism Planning Grant (Note 14)	TRAV			
<b>Total U.S. Appalachian Regional Commission</b>			<b>\$ 1,882,346</b>		<b>\$ 621,161</b>
<b><u>U.S. Equal Employment Opportunity Commission</u></b>					
<b>Direct Programs:</b>					
30.002	Employment Discrimination-State and Local Fair Employment Practices Agency Contracts	HRC	\$ 126,672		
<b>Total U.S. Equal Employment Opportunity Commission</b>			<b>\$ 126,672</b>		
<b><u>U.S. General Services Administration</u></b>					
<b>Direct Programs:</b>					
39.003	Donation of Federal Surplus Personal Property (Note 13)	FAC	\$	\$ 733,042	
39.011	Election Reform Payments (Note 9)	SBE	23,991		
<b>Total U.S. General Services Administration</b>			<b>\$ 23,991</b>	<b>\$ 733,042</b>	
<b><u>U.S. National Foundation on the Arts and the Humanities</u></b>					
<b>Direct Programs:</b>					
45.024	Promotion of the Arts-Grants to Organizations and Individuals	KET	\$ 44,463		\$
45.025	Promotion of the Arts-Partnership Agreements (Note 14)	KAC	531,462		197,291
45.026	Promotion of the Arts-Leadership Initiatives (Note 14)	KHS			
		KAC			
45.129	Promotion of the Humanities-Federal/State Partnership	KHS	8,469		
45.149	Promotion of the Humanities-Division of Preservation and Access	KHS	92,761		
45.310	State Library Program	DLA	1,844,186		444,554
		KET	15,000		
		CPE	8,116		
<b>Passed Through From the Kentucky Humanities Council:</b>					
45.129	Promotion of the Humanities-Federal/State Partnership Pass Through Grantor's #-NA	KET	5,000		
<b>Total U.S. National Foundation on the Arts and Humanities</b>			<b>\$ 2,549,457</b>		<b>\$ 641,845</b>

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA # Program Title		State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<b><u>U.S. Department of Veterans Affairs</u></b>					
<b>Direct Programs:</b>					
64.005	Grants to States for Construction of State Home Facilities	VA	\$ 812,459	\$	
64.114	Veterans Housing-Guaranteed and Insured Loans (Note 2) (Note 3e) (Note 13)	KHCORP			8,941,862
64.203	State Cemetery Grants	VA	1,949,992		
<b>Total U.S. Department of Veterans Affairs</b>			<b>\$ 2,762,451</b>	<b>\$ 8,941,862</b>	
<b><u>U.S. Environmental Protection Agency</u></b>					
<b>Direct Programs:</b>					
66.001	Air Pollution Control Program Support	NREPC	\$ 1,544,473	\$	\$
66.032	State Indoor Radon Grants	CHS	491,601		240,980
66.419	Water Pollution Control State and Interstate Program Support	NREPC	1,547,936		52,229
66.432	State Public Water System Supervision	NREPC	763,700		
66.438	Construction Management Assistance	NREPC	371,451		
66.454	Water Quality Management Planning	NREPC	76,529		15,000
66.458	Capitalization Grants for Clean Water State Revolving Funds (Note 2) (Note 3d) (Note 14)	KIA NREPC	14,826,894		14,541,995
66.460	Nonpoint Source Implementation Grants	NREPC	2,577,438		1,071,333
66.461	Wetland Program Development Grants (Note 14)	F&W NREPC	137,004		
66.463	Water Quality Cooperative Agreements (Note 13)	NREPC	26,564	10,000	25,314
66.467	Wastewater Operator Training Grant Program (Technical Assistance)	NREPC	21,492		
66.468	Capitalization Grants for Drinking Water State Revolving Funds (Note 2) (Note 3d)	KIA NREPC	13,190,005 1,173,469		12,981,122
66.470	Hardship Grants Program for Rural Communities	NREPC	196,423		196,423
66.471	State Grants to Reimburse Operators of Small Water Systems for Training and Certification Costs	NREPC	29,374		
66.474	Water Protection Grants to the States	NREPC	17,061		
66.606	Surveys, Studies, Investigations and Special Purpose Grants (Note 13)	NREPC CHS	367,678 66,935	206,036	10,033 26,367
66.608	State Information Grants (Note 14)	NREPC			
66.700	Consolidated Pesticide Enforcement Cooperative Agreements	AGR	542,597		
66.701	Toxic Substances Compliance Monitoring Cooperative Agreements	NREPC	63,729		10,726
66.707	TSCA Title IV State Lead Grants - Certification of Lead- Based Paint Professionals	CHS	84,908		1,100
66.801	Hazardous Waste Management State Program Support	NREPC	1,534,112		
66.802	Superfund State, Political Subdivision, and Indian Tribe Site- Specific Cooperative Agreements	NREPC	140,412		11,700
66.804	State and Tribal Underground Storage Tanks Program	NREPC	186,675		
66.805	Leaking Underground Storage Tank Trust Fund Program	NREPC	1,267,239		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<b><u>U.S. Environmental Protection Agency (Continued)</u></b>					
<b>Direct Programs (Continued):</b>					
66.809	Superfund State and Indian Tribe Core Program Cooperative Agreements	NREPC	150,681		
66.810	Chemical Emergency Preparedness and Prevention (CEPP) Technical Assistance Grants Program	NREPC	8,069		
<b>Total U.S. Environmental Protection Agency</b>			\$ 41,404,449	\$ 216,036	\$ 29,184,322
<b><u>U.S. Department of Energy</u></b>					
<b>Direct Programs:</b>					
81.039	National Energy Information Center	NREPC	\$ 5,385		\$
81.041	State Energy Program	NREPC	687,273		218,711
81.042	Weatherization Assistance for Low-Income Persons	CFC	4,332,748		4,126,648
		CHS	28,875		
81.079	Regional Biomass Energy Programs (Note 14)	NREPC			
81.086	Conservation Research and Development	NREPC	78,814		25,330
81.089	Fossil Energy Research and Development	M&M	757		
81.106	States and Tribal Concerns, Proposed Solutions	MIL	12,588		
81.117	Energy Efficiency and Renewable Energy Information Dissemination, Outreach, Training and Technical Analysis/Assistance	NREPC	58,288		3,850
81.119	State Energy Program Special Projects	NREPC	204,284		144,022
81.502	Paducah Gaseous Diffusion Plant Environmental Monitoring and Oversight	NREPC	939,675		96,491
		CHS	330,879		170,164
<b>Total U.S. Department of Energy</b>			\$ 6,679,566		\$ 4,785,216
<b><u>U.S. Federal Emergency Management Agency</u></b>					
<b>Direct Programs:</b>					
83.012	Hazardous Materials Assistance Program	MIL	\$ 882		\$
83.105	Community Assistance Program-State Support Services Element (CAP-SSSE)	NREPC	64,610		
83.536	Flood Mitigation Assistance	MIL	302,119		
83.539	Crisis Counseling	MIL	73,576		
83.543	Individual and Family Grants	MIL	312,065		
83.544	Public Assistance Grants (Note 2)	MIL	18,647,654		17,457,980
		TC	1,664,988		
83.548	Hazard Mitigation Grant	MIL	735,770		495,344
83.549	Chemical Stockpile Emergency Preparedness Program	MIL	3,629,829		2,689,715
		CHS	1,095		
83.550	National Dam Safety Program	NREPC	136,872		7,458
83.552	Emergency Management Performance Grants	MIL	1,887,926		660,859
83.556	Fire Management Assistance Grant	MIL	4,353,304		
83.557	Pre-Disaster Mitigation	MIL	49,000		

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**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA # Program Title		State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Federal Emergency Management Agency (Continued)					
Direct Programs (Continued):					
83.562	State and Local All Hazards Emergency Operations Planning	MIL	53,023		
83.563	Emergency Operations Centers	MIL	24,852		
83.564	Citizen Corps	MIL	8,821		
Total U.S. Federal Emergency Management Agency			\$ 31,946,386		\$ 21,311,356
U.S. Department of Education					
Direct Programs:					
84.002	Adult Education-State Grant Program	CWD	\$ 9,928,456		\$ 9,461,406
84.010	Title I Grants to Local Educational Agencies (Note 2)	EDU	129,061,216		124,358,284
84.011	Migrant Education - State Grant Program	EDU	6,962,780		6,812,806
84.013	Title I Program for Neglected and Delinquent Children	JUV	892,035		
		CORR	56,414		
		EDU	9,276		
Special Education Cluster:					
84.027	Special Education - Grants to States (Note 2)	EDU	97,583,762		97,291,280
84.173	Special Education - Preschool Grants (Note 2)	EDU	10,923,826		9,510,745
Student Financial Assistance Programs Cluster:					
84.032	Federal Family Education Loans (Note 2) (Note 3c)	KHEAA	59,420,775		
		KHESLC	13,322,775		
84.048	Vocational Education-Basic Grants to States (Note 2)	CWD	12,739,187		10,921,432
		EDU	6,044,070		5,806,209
84.069	Leveraging Educational Assistance Partnership	KHEAA	914,100		
84.126	Rehabilitation Services-Vocational Rehabilitation Grants to States (Note 2) (Note 9)	CWD	45,504,749		1,001,914
84.128	Rehabilitation Services-Service Projects	CWD	142,024		141,800
84.161	Rehabilitation Services-Client Assistance Program	CWD	149,661		
84.162	Immigrant Education	EDU	332,790		325,939
84.169	Independent Living-State Grants	CWD	248,504		31,575
84.177	Rehabilitation Services-Independent Living Services for Older Individuals Who are Blind	CWD	363,408		
84.181	Special Education-Grants for Infants and Families with Disabilities (Note 14)	CCSHCN	5,565,602		
		CHS			
84.185	Byrd Honors Scholarships	EDU	527,695		
84.186	Safe and Drug-Free Schools and Communities-State Grants	EDU	4,858,961		4,803,160
		CHS	531,284		499,507
		KSP	42,484		
		GOV	32,652		
84.187	Supported Employment Services for Individuals with Severe Disabilities	CWD	431,381		
84.194	Bilingual Education Support Services	EDU	25,298		

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State	Expenditures		Provided to Subrecipient
		Organizations	Cash	Noncash	
U.S. Department of Education (Continued)					
Direct Programs (Continued):					
84.196	Education for Homeless Children and Youth	EDU	657,306		651,777
84.203	Star Schools (Note 14)	KET			
84.213	Even Start - State Educational Agencies	EDU	2,979,973		2,752,575
84.215	Fund for the Improvement of Education	EDU	14,108		
84.216	Capital Expenses	EDU	65,256		65,256
84.224	Assistive Technology	CWD	409,016		207,420
84.240	Program of Protection and Advocacy of Individual Rights	PUBAD	197,089		
84.243	Tech-Prep Education	CWD	2,659,674		2,478,387
84.265	Rehabilitation Training-State Vocational Rehabilitation Unit In-Service Training	CWD	91,355		
84.276	Goals 2000 - State and Local Education Systemic Improvement Grants	EDU	164,035		7,878
84.281	Eisenhower Professional Development State Grants (Note 2)	EDU	4,304,463		3,850,351
		CPE	1,000,586		989,960
84.287	Twenty-First Century Community Learning Centers	EDU	2,145,074		2,107,721
84.293	Foreign Language Assistance	EDU	60,064		13,306
84.298	Innovative Education Program Strategies	EDU	3,748,020		3,517,053
		KCA	25,000		
84.314	Even Start - Statewide Family Literacy Program	EDU	270,499		
84.318	Education Technology State Grants	EDU	1,231,722		1,050,470
84.323	Special Education-State Program Improvement Grants for Children with Disabilities	EDU	543,421		523,606
		CHS	13,115		
84.326	Special Education - Technical Assistance and Dissemination to Improve Services and Results for Children with Disabilities	EDU	66,631		54,684
84.330	Advanced Placement Program	EDU	546,432		126,544
84.331	Grants to States for Incarcerated Youth Offenders	CORR	142,557		
84.332	Comprehensive School Reform Demonstration	EDU	3,847,136		3,720,368
84.334	Gaining Early Awareness and Readiness for Undergraduate Programs (Note 2)	CPE	1,975,340		1,333,537
84.336	Teacher Quality Enhancement Grants	EPSB	299,551		
84.338	Reading Excellence	EDU	1,415,957		1,354,621
84.340	Class Size Reduction	EDU	10,261,862		10,261,860
84.343	Assistive Technology - State Grants for Protection and Advocacy	PUBAD	102,379		
84.346	Vocational Education-Occupational and Employment Information State Grants	CWD	83,690		
84.348	Title I Accountability Grants	EDU	2,785,212		2,785,211
84.352	School Renovation Grants	EDU	8,800,000		8,800,000
84.358	Rural Education	EDU	1,789,292		1,789,292
84.365	English Language Acquisition Grants	EDU	366,403		365,351
84.367	Improving Teacher Quality State Grants	EDU	11,459,257		11,434,831
		CPE	11,309		
84.369	Grants for State Assessments and Related Activities	EDU	4,565,332		69,801

See accompanying Notes to the Schedule of Expenditures of Federal Awards



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<b><u>U.S. Department of Education (Continued)</u></b>					
<b>Passed Through From the Harlan Independent Board of Education:</b>					
84.215	Fund for the Improvement of Education Pass Through Grantor's #S215X020143	KHS	69,970		
<b>Total U.S. Department of Education</b>			\$ 475,783,251		\$ 331,277,917
<b><u>U.S. National Archives and Records Administration</u></b>					
<b>Direct Programs:</b>					
89.003	National Historical Publications and Records Grants	DLA	\$ 718		
<b>Total U.S. National Archives and Records Administration</b>			\$ 718		
<b><u>U.S. Department of Health and Human Services</u></b>					
<b>Direct Programs:</b>					
93.003	Public Health and Social Services Emergency Fund	CHS	\$ 123,659	\$	\$ 20,277
93.041	Special Programs for the Aging - Title VII, Chapter 3 - Programs for Prevention of Elder Abuse, Neglect, and Exploitation	CHS	74,366		73,728
93.042	Special Programs for the Aging - Title VII, Chapter 2 - Long Term Care Ombudsman Services for Older Individuals	CHS	180,603		95,418
93.043	Special Programs for the Aging - Title III, Part D - Disease Prevention and Health Promotion Services	CHS	245,559		243,520
<b>Aging Cluster:</b>					
93.044	Special Programs for the Aging - Title III, Part B - Grants for Supportive Services and Senior Centers	CHS	4,947,835		4,937,070
93.045	Special Programs for the Aging - Title III, Part C - Nutrition Services	CHS	7,648,793		7,383,980
93.046	Special Programs for the Aging - Title III, Part D - In-Home Services for Frail Older Individuals (Note 14)	CHS			
93.048	Special Programs for the Aging - Title IV and Title II- Discretionary Projects	CHS	28,373		28,373
93.052	National Family Caregiver Support	CHS	1,476,953		1,375,674
93.053	Nutrition Services Incentive Program	CHS	653,597		653,597
93.104	Comprehensive Community Mental Health Services for Children with Serious Emotional Disturbances (SED)	CHS	1,149,422		1,143,882
93.110	Maternal and Child Health Federal Consolidated Programs	CCSHCN	461,430		
		CHS	56,590		16,000
93.116	Project Grants and Cooperative Agreements for Tuberculosis Control Programs (Note 13)	CHS	1,049,791	52,602	864,585
93.127	Emergency Medical Services for Children	EMSB	107,372		
93.130	Primary Care Services - Resource Coordination and Development	CHS	94,374		30,000

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of Health and Human Services (Continued)					
Direct Programs (Continued):					
93.136	Injury Prevention and Control Research and State and Community Based Programs	CHS	1,043,500		1,033,196
93.138	Protection and Advocacy for Individuals with Mental Illness	PUBAD	403,701		
93.150	Projects for Assistance In Transition from Homelessness (PATH)	CHS	300,000		300,000
93.197	Childhood Lead Poisoning Prevention Projects - State and Local Childhood Lead Poisoning Prevention and Surveillance of Blood Lead Levels in Children	CHS	236,022		78,514
93.217	Family Planning - Services	CHS	5,339,464		5,083,488
93.230	Consolidated Knowledge Development and Application (KD&A) Program (Note 9)	CHS	657,824		602,866
93.234	Traumatic Brain Injury-State Demonstration Grant Program	PUBAD	50,000		
93.235	Abstinence Education	CHS	950,126		893,553
93.238	Cooperative Agreements for State Treatment Outcomes and Performance Pilot Studies Enhancement (Note 9)	CHS	434,714		347,125
93.251	Universal Newborn Hearing Screening	CCSHCN	138,199		
93.262	Occupational Safety and Health Research Grants	CHS	18,897		18,897
93.268	Immunization Grants (Note 13)	CHS	2,498,134	12,775,047	1,834,719
93.283	Centers for Disease Control and Prevention-Investigations and Technical Assistance (Note 13)	CHS	8,575,216	49,343	5,657,368
		CCSHCN	182,944		
		MIL	113,077		
93.556	Promoting Safe and Stable Families	CFC	5,123,702		4,217,434
		CHS	378		
93.558	Temporary Assistance for Needy Families (Note 2)	CFC	116,806,920		11,227,169
		CWD	2,816,207		
		KHCORP	720,756		
		OAG	385,000		
		CHS	168,623		
93.563	Child Support Enforcement (Note 2)	CFC	40,393,975		32,316,177
		OAG	138,506		
		CHS	5,903		
93.568	Low-Income Home Energy Assistance (Note 2)	CFC	27,987,481		27,848,559
		CHS	9,933		
93.569	Community Services Block Grant	CFC	10,864,528		10,294,649
		CHS	34,757		
93.571	Community Services Block Grant Discretionary Awards-Community Food and Nutrition	CFC	73,235		73,235
Child Care Cluster:					
93.575	Child Care and Development Block Grant (Note 2)	CFC	95,160,956		11,851,195
93.596	Child Care Mandatory and Matching Funds of the Child Care and Development Fund (Note 2)	CFC	29,958,144		14,910
		CHS	2,493,243		
93.576	Refugee and Entrant Assistance - Discretionary Grants	EDU	310,573		308,329
93.585	Empowerment Zones Program	FAC	1,032,594		1,032,594

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2003**  
**(CONTINUED)**

CFDA #	Program Title	State	Expenditures		Provided to Subrecipient
		Organizations	Cash	Noncash	
U.S. Department of Health and Human Services (Continued)					
Direct Programs (Continued):					
93.586	State Court Improvement Program	AOC	137,051		
93.590	Community-Based Family Resource and Support Grants	CFC	1,318,364		1,115,858
		AOC	19,734		
93.597	Grants to States for Access and Visitation Programs	CFC	162,502		162,502
93.600	Head Start	GOV	171,561		
93.603	Adoption Incentive Payments	CFC	1,324,531		
93.630	Developmental Disabilities Basic Support and Advocacy Grants	CHS	935,782		537,245
		PUBAD	509,168		
		CWD	27,190		
93.643	Children's Justice Grants to States (Note 14)	CFC	219,781		138,105
		AOC	67,145		
		OAG			
93.645	Child Welfare Services-State Grants	CFC	4,662,098		
93.658	Foster Care-Title IV-E (Note 2)	CFC	53,314,780		25,344
		JUV	1,935,332		
		AOC	229,640		
		CHS	96,073		
93.659	Adoption Assistance	CFC	15,419,944		
93.667	Social Services Block Grant (Note 2)	CFC	17,096,491		903,887
		JUV	7,677,969		
		CHS	181,802		168,378
93.669	Child Abuse and Neglect State Grants (Note 14)	CFC	338,689		143,693
		OAG			
93.671	Family Violence Prevention and Services-Grants for Battered Women's Shelters-Grants to States and Indian Tribes	CFC	1,675,989		1,666,640
		CHS	212		
93.674	Chafee Foster Care Independent Living	CFC	1,115,460		878,076
		CHS	103		
93.767	State Children's Insurance Program (Note 2)	CHS	69,880,862		312,295
		CFC	356,629		
Medicaid Cluster:					
93.775	State Medicaid Fraud Control Units (Note 2)	OAG	983,713		
93.777	State Survey and Certification of Health Care Providers and Suppliers (Note 2)	CHS	5,782,711		
93.778	Medical Assistance Program (Note 2)	CHS	2,735,768,588		
		CFC	17,020,069		
		OAG	106,501		
93.779	Centers for Medicare and Medicaid Services (CMS) Research, Demonstrations and Evaluations	CHS	794,870		630,179
		KHCORP	45,000		
93.917	HIV Care Formula Grants	CHS	6,747,313		5,075,336
93.919	Cooperative Agreements for State-Based Comprehensive Breast and Cervical Cancer Early Detection Programs	CHS	877,572		787,422

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA #	Program Title	State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
U.S. Department of Health and Human Services (Continued)					
Direct Programs (Continued):					
93.938	Cooperative Agreements to Support Comprehensive School Health Programs to Prevent the Spread of HIV and Other Important Health Problems	EDU	235,255		136,648
93.940	HIV Prevention Activities - Health Department Based (Note 13)	CHS	2,114,339	11,599	1,099,819
93.944	Human Immunodeficiency Virus (HIV)/Acquired Immunodeficiency Virus Syndrome (AIDS) Surveillance	CHS	106,308		39,484
93.945	Assistance Programs for Chronic Disease Prevention and Control	CHS	860,317		220,499
		EDU	272,711		251,666
93.952	Improving EMS/Trauma Care in Rural Areas	EMSB	46,293		
93.958	Block Grants for Community Mental Health Services	CHS	5,960,002		5,876,657
		CWD	81,665		
		CORR	50,000		
93.959	Block Grants for Prevention and Treatment of Substance Abuse (Note 2)	CHS	21,918,102		21,746,559
		AOC	322,674		81,529
		CORR	175,000		
93.977	Preventive Health Services - Sexually Transmitted Diseases Control Grants (Note 13)	CHS	1,026,720	333,506	221,485
93.988	Cooperative Agreements for State-Based Diabetes Control Programs and Evaluation of Surveillance Systems	CHS	532,250		468,375
93.991	Preventive Health and Health Services Block Grant	CHS	1,795,984		1,671,519
93.994	Maternal and Child Health Services Block Grant to the States	CHS	8,078,161		8,024,892
		CCHSHCN	4,384,276		
NA	The Placement and Treatment of Neuropsychiatric Patients (Note 14)	CFC			
Passed Through From the University of Kentucky:					
93.241	State Rural Hospital Flexibility Program Pass Through Grantor's #-Various	EMSB	360,000		360,000
93.259	Rural Access to Emergency Devices Grant (Note 14) Pass Through Grantor's #-1 H3D RH 00005-01 4-66435-03-253	EMSB			
Total U.S. Department of Health and Human Services			\$ 3,369,047,225	\$ 13,222,097	\$ 184,644,173
U.S. Corporation for National and Community Service					
Direct Programs:					
94.003	State Commissions	CFC	\$ 153,271		\$
94.004	Learn and Serve America-School and Community Based Programs (Note 14)	EDU	417,411		386,017
		CFC			
94.006	AmeriCorps	CFC	3,050,320		3,049,776
94.007	Planning and Program Development Grants	CFC	27,134		14,516
		JUV	14,741		
94.009	Training and Technical Assistance	CFC	42,825		19,138

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

CFDA # Program Title		State Organizations	Expenditures		Provided to Subrecipient
			Cash	Noncash	
<b><u>U.S. Corporation for National and Community Service (Continued)</u></b>					
<b>Direct Programs (Continued):</b>					
<b>Foster Grandparents/Senior Companion Cluster:</b>					
94.011	Foster Grandparent Program	CHS	546,121		108,325
NA	Chemical Laboratory Improvement Act	CHS	246,161		
<b>Total U.S. Corporation for National and Community Service</b>			<b>\$ 4,497,984</b>		<b>\$ 3,577,772</b>
<b><u>U.S. Office of National Drug Control Policy</u></b>					
NA	HIDTA Program	KSP	\$ 656,039		
<b>Total U.S. Office of National Drug Control Policy</b>			<b>\$ 656,039</b>		
<b><u>U.S. Social Security Administration</u></b>					
<b>Direct Programs:</b>					
<b>Disability Insurance/SSI Cluster:</b>					
96.001	Social Security-Disability Insurance (Note 2)	CFC	\$ 38,278,470		
96.008	Social Security - Benefits Planning, Assistance, and Outreach Program	PUBAD	100,765		
<b>Total U.S. Social Security Administration</b>			<b>\$ 38,379,235</b>		
<b><u>Other Federal Assistance</u></b>					
<b>Direct Programs:</b>					
NA	Appalachia High Intensity Drug Trafficking Area	GOV	\$ 31,734		\$
NA	Joint Funding Administration (Note 8)	DLG	1,683,000		1,683,000
<b>Total Other Federal Assistance</b>			<b>\$ 1,714,734</b>		<b>\$ 1,683,000</b>
<b>Total All State Organizations</b>			<b>\$ 5,815,538,953</b>	<b>\$ 708,779,324</b>	<b>\$ 887,379,387</b>

See accompanying Notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF KENTUCKY**  
**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2003**

**Note 1 - Purpose of the Schedule and Significant Accounting Policies**

**Basis of Presentation** - OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requires a Schedule of Expenditures of Federal Awards showing each federal financial assistance program as identified in the *Catalog of Federal Domestic Assistance*. The accompanying schedule includes all federal grant activity for the Commonwealth, except those programs administered by state universities, and is presented primarily on the basis of cash disbursements as modified by the application of Kentucky Revised Statute (KRS) 45.229. Consequently, certain expenditures are recorded in the accounts only when cash is disbursed. The Commonwealth elected to exclude state universities from the statewide single audit, except as part of the audit of the basic financial statements.

KRS 45.229 provides that the Finance and Administration Cabinet may, “for a period of thirty (30) days after the close of any fiscal year, draw warrants against the available balances of appropriations made for that fiscal year, for the payment of expenditures incurred during that year or in fulfillment of contracts properly made during the year, but for no other purpose.” However, there is an exception to the application of KRS 45.229 in that regular payroll expenses incurred during the last pay period of the fiscal year are charged to the next year.

The basic financial statements of the Commonwealth are presented on the modified accrual basis of accounting for the governmental fund financial statements and the accrual basis of accounting for the government-wide, proprietary fund, and fiduciary fund financial statements. Therefore, the schedule may not be directly traceable to the basic financial statements in all cases.

Noncash assistance programs are not reported in the basic financial statements of the Commonwealth for FY 03. The noncash expenditures presented on this schedule represent the noncash assistance expended using the method or basis of valuation described in Note 13.

Clusters of programs are indicated in the schedule by light gray shading.

The state agencies’ schedule is presented on the cash, modified cash, or accrual basis of accounting.

**Inter-Agency Activity** - Certain transactions relating to federal financial assistance may appear in the records of more than one (1) state agency. To avoid the overstatement of federal expenditures, the following policies were adopted for the presentation of the schedule:

**COMMONWEALTH OF KENTUCKY**  
**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2003**  
**(CONTINUED)**

**Note 1 - Purpose of the Schedule and Significant Accounting Policies (Continued)**

**Inter-Agency Activity (Continued)**

(a) Federal moneys may be received by a state agency and passed through to another state agency where the moneys are expended. Except for pass-throughs to state universities as discussed below, this inter-agency transfer activity is reported by the agency expending the moneys.

State agencies that pass federal funds to state universities report those amounts as expenditures.

(b) Federal moneys received by a state agency and used to purchase goods or services from another state agency are reported in the schedule as an expenditure by the purchasing agency only.

**Note 2 - Type A Programs**

Type A programs for the Commonwealth mean any program for which total expenditures of federal awards exceeded \$18 million for FY 03. The Commonwealth had the following programs (cash and noncash) that met the Type A program definition for FY 03, some of which were administered by more than one (1) state agency. Certain component units and agencies audited by certified public accounting firms had lower dollar thresholds. The Commonwealth identified clusters among the Type A programs by gray shading. These Type A programs and clusters were:

<b>CFDA #</b>	<b>Program Title</b>	<b>Expenditures</b>
<b>Food Stamp Cluster:</b>		
<b>10.551</b>	Food Stamps	\$ 467,646,178
<b>10.561</b>	State Administrative Matching Grants for Food Stamp Program	26,106,666
<b>Child Nutrition Cluster:</b>		
<b>10.553</b>	School Breakfast Program	31,442,100
<b>10.555</b>	National School Lunch Program	96,865,656
<b>10.556</b>	Special Milk Program for Children	93,914
<b>10.559</b>	Summer Food Service Program for Children	4,532,272
<b>10.557</b>	Special Supplemental Nutrition Program for Women, Infants, and Children	80,187,442
<b>10.558</b>	Child and Adult Care Food Program	25,044,722
<b>10.766</b>	Community Facilities Loans and Grants	67,738,386

**COMMONWEALTH OF KENTUCKY**  
**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2003**  
**(CONTINUED)**

**Note 2 - Type A Programs (Continued)**

<b>CFDA #</b>	<b>Program Title</b>	<b>Expenditures</b>
<b>11.550</b>	Public Telecommunications Facilities-Planning and Construction	462,090
<b>14.117</b>	Mortgage Insurance – Homes	128,206,362
<b>Section 8 Project-Based Cluster:</b>		
<b>14.182</b>	Lower Income Housing Assistance Program – Section 8 New Construction/Substantial Rehabilitation	84,569,085
<b>14.856</b>	Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation	240,015
<b>14.228</b>	Community Development Block Grants/State’s Program	31,661,755
<b>14.235</b>	Supportive Housing Program	3,245,684
<b>14.239</b>	HOME Investment Partnerships Program	17,182,667
<b>14.871</b>	Section 8 Housing Choice Vouchers	20,485,291
<b>17.225</b>	Unemployment Insurance	640,076,477
<b>17.245</b>	Trade Adjustment Assistance-Workers	18,516,129
<b>17.255</b>	Workforce Investment Act	109,196
<b>Workforce Investment Act Cluster:</b>		
<b>17.258</b>	WIA Adult Program	13,537,375
<b>17.259</b>	WIA Youth Activities	15,210,786
<b>17.260</b>	WIA Dislocated Workers	19,565,986
<b>Highway Planning and Construction Cluster:</b>		
<b>20.205</b>	Highway Planning and Construction	485,248,928
<b>21.999</b>	Job Growth Tax Relief Reconciliation Act	68,720,606
<b>64.114</b>	Veterans Housing-Guaranteed and Insured Loans	8,941,862
<b>66.458</b>	Capitalization Grants for Clean Water State Revolving Funds	14,826,894
<b>66.468</b>	Capitalization Grants for Drinking Water State Revolving Funds	14,363,474
<b>83.544</b>	Public Assistance Grants	20,312,642
<b>84.010</b>	Title I Grants to Local Educational Agencies	129,061,216



**COMMONWEALTH OF KENTUCKY**  
**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2003**  
**(CONTINUED)**

**Note 2 - Type A Programs (Continued)**

<b>CFDA #</b>	<b>Program Title</b>	<b>Expenditures</b>
<b>Special Education Cluster:</b>		
<b>84.027</b>	Special Education - Grants to States	97,583,762
<b>84.173</b>	Special Education – Preschool Grants	10,923,826
<b>Student Financial Assistance Program Cluster:</b>		
<b>84.032</b>	Federal Family Education Loans	72,743,550
<b>84.048</b>	Vocational Education-Basic Grants to States	18,783,257
<b>84.126</b>	Rehabilitation Services – Vocational Rehabilitation Grants to States	45,504,749
<b>84.281</b>	Eisenhower Professional Development State Grants	5,305,049
<b>84.334</b>	Gaining Early Awareness and Readiness for Undergraduate Programs	1,975,340
<b>93.558</b>	Temporary Assistance for Needy Families	120,897,506
<b>93.563</b>	Child Support Enforcement	40,538,384
<b>93.568</b>	Low-Income Home Energy Assistance	27,997,414
<b>Child Care Cluster:</b>		
<b>93.575</b>	Child Care and Development Block Grant	95,160,956
<b>93.596</b>	Child Care Mandatory and Matching Funds of the Child Care and Development Fund	32,451,387
<b>93.658</b>	Foster Care-Title IV-E	55,575,825
<b>93.667</b>	Social Services Block Grant	24,956,262
<b>93.767</b>	State Children’s Insurance Program	70,237,491
<b>Medicaid Cluster:</b>		
<b>93.775</b>	State Medicaid Fraud Control Units	983,713
<b>93.777</b>	State Survey and Certification of Health Care Providers and Suppliers	5,782,711
<b>93.778</b>	Medical Assistance Program	2,752,895,158
<b>93.959</b>	Block Grants for Prevention and Treatment of Substance Abuse	22,415,776
<b>Disability Insurance/SSI Cluster:</b>		
<b>96.001</b>	Social Security – Disability Insurance	38,278,470
<b>Total Type A Programs</b>		<b>\$ 6,075,192,442</b>

**COMMONWEALTH OF KENTUCKY  
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**Note 3 - Federally Assisted Loan Programs**

The Commonwealth has several loan programs made possible with initial advances in prior years from the federal government. In addition, the federal government guarantees some loan programs.

a) The Kentucky Rural Rehabilitation Student Loan Program was initially awarded \$672,629 in 1970 by the U. S. Farmers Home Administration. Since 1970, the program has operated on interest from student loans outstanding and on income from investments administered by the Office of Financial Management. The Department of Agriculture is no longer in the business of making student loans and reassigned all loans in payment compliance to the Kentucky Higher Education Assistance Authority (KHEAA). The Department of Agriculture retained only those loans that had a delinquent payment history. This program is currently in phase-out status, with authorization from the U. S. Department of Agriculture (USDA) to eliminate the principal through issuance of specific grants and scholarships. Most outstanding loans have been classified as contingent uncollectible liabilities. When loan payments are received, they are directly deposited into the principal account. The total amount of money in the investment account as of June 30, 2003 was \$734,948. Student loans and investment earned interest of \$44,517. Outstanding student loans totaled \$64,466. The total grants and scholarships authorized by the USDA in FY 03 totaled \$114,232.

b) Total moneys for the Gas System Restoration Project, administered by the Department for Local Government (CFDA #11.307), consist of \$3,150,000 from the U.S. Economic Development Administration; \$500,000 from the U.S. Appalachian Regional Commission; and, \$650,000 in state matching money, for a total commitment to the revolving loan program of \$4,300,000. All monies had been received and paid out by June 30, 2003. In addition, principal and interest repaid is available for lending.

c) The Kentucky Higher Education Student Loan Corporation (KHESLC) issues revenue bonds in order to purchase student loans authorized under the Federal Family Education Loans program (CFDA #84.032). The KHEAA guarantees substantially all loans made and purchased by the KHESLC. The U.S. Department of Education provides for reinsurance of loans guaranteed by the KHEAA. Outstanding loans guaranteed under this program totaled \$2,602,905,000 as of June 30, 2003.

d) The Kentucky Infrastructure Authority administers wastewater revolving loan programs (CFDA #66.458 and 66.468) funded by the U.S. Environmental Protection Agency's Capitalization Grants for State Revolving Funds. During the year ended June 30, 2003, the Authority issued loans totaling \$27,523,117, with outstanding loans of \$263,527,774 at year-end.

**COMMONWEALTH OF KENTUCKY**  
**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2003**  
**(CONTINUED)**

**Note 3 - Federally Assisted Loan Programs (Continued)**

e) The Department of Housing and Urban Development's Mortgage Insurance-Homes (CFDA #14.117), Department of Agriculture's Community Facilities Loans and Grants (CFDA #10.766), and Department of Veterans Affairs' Veterans Housing-Guaranteed and Insured Loans (CFDA #64.114) represent the loans originated in FY 03 by the Kentucky Housing Corporation. The cumulative outstanding balance of the Mortgage Insurance Program, Community Facilities Loans and Grants Program, and Veterans Housing and Guaranteed Loans Program loans originated by the Kentucky Housing Corporation is \$704,859,143, \$277,960,985, and \$65,766,125, respectively at June 30, 2003.

**Note 4 - Activity Occurring in Programs with Inventoriable Items**

The Department of Agriculture operates a warehouse in Louisville, Kentucky for the Commodity Supplemental Food Program (CFDA #10.565). The dollar value of the inventory, based on the USDA Commodity File dated July 2003 is as follows:

	<b>Commodity Supplemental Food Program CFDA #10.565</b>	
Beginning Inventory, July 1, 2002	\$	567,538
Received		1,253,949
Issued to Recipients		(1,395,394)
Ending Inventory, June 30, 2003	\$	426,093

**Note 5 - Unemployment Insurance (CFDA #17.225)**

The Commonwealth paid out \$611,175,296 in benefits in FY 03. The amounts shown on the accompanying schedule reflect both the amount expended for benefits from the Trust Fund and an additional \$28,901,181 of federal funds expended for administration of the program, resulting in a combined total of \$640,076,477 in federal expenditures.

**Note 6 - Highway Planning and Construction (CFDA #20.205)**

The information reported for this program represents the activity of all open projects during FY 03. These projects were funded from several apportionments. Apportionments refer to a federal, statutorily prescribed division or assignment of

**COMMONWEALTH OF KENTUCKY  
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**Note 6 - Highway Planning and Construction (CFDA #20.205) (Continued)**

funds. The expenditures reflected on the schedule include expenditures for advance construction projects, which are not yet under agreements with the Federal Highway Administration.

Program Income - The Highway Planning and Construction Program earned program income of \$447,466 in FY 03. This income was earned in the right-of-way phase through the sale and rental of real property. Income earned in this manner was classified as a negative expenditure, resulting in a reduction to federal expenditures for the current year.

Refunds - Expenditures for the Highway Planning and Construction Program were shown net of any refunds, resulting from a reimbursement of prior or current year expenditures. Refunds totaled \$3,444,491 for FY 03.

**Note 7 - Outdoor Recreation - Acquisition, Development and Planning  
(CFDA # 15.916) and Recreational Trails Program (CFDA # 20.219)**

Administrative costs are shown as expended when received from the federal government. These costs are recovered through a negotiated, fixed-indirect cost rate. Any over or under recovery will be recouped in the future.

**Note 8 - Joint Funding Administration**

The Joint Funding Administration Program (listed in the schedule under Other Federal Assistance) consists of grants from the following federal agencies:

- U.S. Department of Commerce
- U.S. Department of Housing and Urban Development
- U.S. Appalachian Regional Commission

**Note 9 - Research and Development Expenditures**

OMB Circular A-133 Section 105 states, "Research and development (R&D) means all research activities, both basic and applied, and all development activities that are performed by a non-federal entity."

The expenditures presented in the SEFA include R&D expenditures. The R&D portion of the expenditures for each program is listed below.

**COMMONWEALTH OF KENTUCKY  
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**Note 9 - Research and Development Expenditures (Continued)**

<b>CFDA #</b>	<b>Program Title</b>	<b>State Organization</b>	<b>Expenditures</b>
10.028	Wildlife Services	F&W	\$ 17,988
15.605	Sport Fish Restoration	F&W	1,269,540
15.615	Cooperative Endangered Species Conservation Fund	F&W	103,689
15.625	Wildlife Conservation and Restoration	F&W	66,408
15.634	State Wildlife Grants	F&W	152,905
16.585	Drug Court Discretionary Grant Program	AOC	73,828
39.011	Election Reform Payments	BOE	23,991
84.126	Rehabilitation Services-Vocational Rehabilitation Grants to States	CWD	61,815
93.230	Consolidated Knowledge Development and Application (KD&A) Program	CHS	308,131
93.238	Cooperative Agreements for State Treatment Outcomes and Performance Pilot Studies Enhancement	CHS	210,629
<b>Total R&amp;D Expenditures</b>			<u>\$ 2,288,924</u>

**Note 10 - Community Development Block Grants/State's Program (CFDA #14.228)**

The Commonwealth matches the federal portion of administration dollar for dollar. Cash expenditures include the federal portion of administration.

**Note 11 - Wildlife Restoration (CFDA #15.611)**

The Department of Fish and Wildlife Resources leases properties from the U.S. Army Corp of Engineers for Condition Three and Condition Five Projects. These projects stipulate that the properties leased be managed for wildlife purposes and may produce income. The leases for wildlife management rights on these properties are non-monetary. The Department of Fish and Wildlife Resources currently leases the following properties:

- Barren River
- Green River
- Dewey Lake
- Fishtrap Lake

**COMMONWEALTH OF KENTUCKY  
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**Note 11 - Wildlife Restoration (CFDA #15.611) (Continued)**

Any expenditure in excess of revenue from each property listed above will be eligible for reimbursement under the Wildlife Restoration grant (CFDA # 15.611) from the U.S. Department of the Interior. The properties listed above are not reimbursed with federal funds, if the grant has already been expended to manage other wildlife properties.

**Note 12 - Workforce Investment Act (CFDA #17.255) and WIA Dislocated Workers (CFDA 17.260)**

The Workforce Investment Act program (CFDA #17.255) reports total cash expenditures of \$109,196. This amount includes expenditures of \$102,574 and \$6,622 from the Job Training Partnership Act (CFDA #17.250) and CFDA #17.255, respectively. These programs were consolidated into the WIA Adult Program (CFDA #17.258) and WIA Youth Activities (CFDA #17.259) in 2001. However, the expenditures cannot be accounted for separately by the agency and, therefore, will be reported under CFDA #17.255 until fully expended.

WIA Dislocated Workers (CFDA #17.260) includes cash expenditures of \$4,074,341 from the Employment and Training Assistance – Dislocated Workers (CFDA #17.246) grant. CFDA #17.246 was consolidated into CFDA #17.260 in 2001.

**Note 13 - Noncash Expenditure Programs**

The Commonwealth's noncash programs and a description of the method/basis of valuation follow.

<b>CFDA #</b>	<b>Program Title</b>	<b>Amount</b>	<b>Method/Basis of Valuation</b>
10.550	Food Donation	\$ 13,474,504	Quantity issued to recipients ECOS Report dated October 1, 2003.
10.551	Food Stamps	467,646,178	Electronic Benefit Transfer Issuance.
10.565	Commodity Supplemental Food Program	1,395,394	Quantity issued to recipients valued at USDA's July 2003 prices.
10.569	Emergency Food Assistance Program (Food Commodities)	6,753,576	Quantity issued to recipients valued at USDA's April 2003 prices.

**COMMONWEALTH OF KENTUCKY  
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**Note 13 - Noncash Expenditure Programs (Continued)**

<b>CFDA #</b>	<b>Program Title</b>	<b>Amount</b>	<b>Method/Basis of Valuation</b>
10.664	Cooperative Forestry Assistance	327,265	Determined by Federal government.
10.766	Community Facilities Loans and Grants	67,738,386	Book value of loans.
10.914	Wildlife Habitat Incentive Program	15,750	75% of agreement total (\$21,000).
14.117	Mortgage Insurance-Homes	128,206,362	Book value of loans.
15.252	Abandoned Mine Land Reclamation (AMLR) Program	50,372	Inventory of controlled property.
15.808	U.S. Geological Survey - Research and Data Acquisition	58,500	Half of investigation cost at Maxey Flats.
39.003	Donation of Federal Surplus Personal Property	733,042	23.3% of federal acquisition cost (\$3,146,103).
64.114	Veterans Housing - Guaranteed and Insured Loans	8,941,862	Book value of loans.
66.463	Water Quality Cooperative Agreements	10,000	The Division of Water received periodic Progress Reports from the EPA documenting activities and deliverables.
66.606	Surveys, Studies, Investigations and Special Purpose Grants	206,036	EPA and National Parks air monitoring contract and actual cost of filters purchased by EPA for NREPC.
93.116	Project Grants and Cooperative Agreements for Tuberculosis Control Programs	52,602	Per authorized award for personnel costs and travel.

**COMMONWEALTH OF KENTUCKY  
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**Note 13 - Noncash Expenditure Programs (Continued)**

<b>CFDA #</b>	<b>Program Title</b>	<b>Amount</b>	<b>Method/Basis of Valuation</b>
93.268	Immunization Grants	12,775,047	Per authorized award for personnel, vaccine costs, and travel.
93.283	Centers for Disease Control and Prevention-Investigations and Technical Assistance	49,343	Per authorized award.
93.940	HIV Prevention Activities - Health Department Based	11,599	Per authorized award.
93.977	Preventive Health Services - Sexually Transmitted Diseases Control Grants	333,506	Per authorized award.
<b>Total Noncash Expenditures</b>		<u>\$ 708,779,324</u>	

**Note 14 - Zero Expenditure Programs**

These programs had no expenditures related to the respective state organization during FY 03. The zero expenditure programs included programs with no activity during the year, such as old programs not officially closed out or new programs issued late in the fiscal year. They also included programs with activity other than expenditures. For CFDA numbers with multiple state organizations listed, the schedule is presented in descending expenditure amount order.

**Note 15 - Noncompliance Item-Highway Planning and Construction (CFDA #20.205)**

The Transportation Cabinet has been informed by the Kentucky Office of Federal Highway Administration that its method of charging certain costs to federal programs is in violation of OMB Circular A-87. These costs involve charges that could possibly be classified as indirect costs. The Transportation Cabinet has implemented changes in their accounting procedures to eliminate these type charges from the federal billing.



## **REPORTS ON COMPLIANCE AND ON INTERNAL CONTROL**



CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS

Report on Compliance and on Internal Control Over Financial Reporting  
Based on an Audit of Financial Statements  
Performed in Accordance With  
*Government Auditing Standards*

Honorable Ernie Fletcher, Governor  
Cabinet Secretaries and Agency Heads  
Members of the Commonwealth of Kentucky Legislature

We have audited the financial statements of the governmental activities, business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth of Kentucky as of and for the year ended June 30, 2003, which collectively comprise the Commonwealth's basic financial statements and have issued our report thereon dated December 23, 2003. Several agencies were tested for compliance and internal control requirements in accordance with *Government Auditing Standards* by other auditors, whose reports thereon have been furnished to us. However, the audit reports for Eastern Kentucky University and Kentucky State University have not been released as of the date of this report and therefore those financial statements have not been audited.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Commonwealth's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and questioned costs as item 03-FAC2-4. We also noted certain immaterial instances of noncompliance, which we have reported to management.

Report on Compliance and on Internal Control Over  
Financial Reporting Based on an Audit of  
Financial Statements Performed in Accordance  
With *Government Auditing Standards*  
(Continued)

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Commonwealth's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Commonwealth's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 03-CFC1-1, 03-CFC2-2, 03-FAC1-3, 03-FAC2-4, 03-FAC3-5, 03-FAC4-6, 03-FAC5-7, 03-FAC6-8, 03-FAC7-9, 03-FAC8-10, 03-CHS1-11, 03-CHS2-12, 03-REV1-13, 03-REV2-14, 03-REV3-15, 03-REV4-16, 03-REV5-17, 03-TC1-18, 03-TC2-19, 03-TC3-20, 03-TC4-21, 03-TC5-22, 03-TC6-23, 03-TC8-24, 03-CWD1-25, 03-CWD2-26, and 03-CWD3-27.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to management.

Report on Compliance and on Internal Control Over  
Financial Reporting Based on an Audit of  
Financial Statements Performed in Accordance  
With *Government Auditing Standards*  
(Continued)

This report is intended solely for the information and use of management, members of the legislature, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in black ink, appearing to read 'Crit Luallen', with a long horizontal flourish extending to the right.

Crit Luallen  
Auditor of Public Accounts

December 23, 2003



CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS

Report on Compliance With Requirements Applicable to Each  
Major Program and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133 and on the  
Schedule of Expenditures of Federal Awards

Honorable Ernie Fletcher, Governor  
Cabinet Secretaries and Agency Heads  
Members of the Commonwealth of Kentucky Legislature

Compliance

We have audited the compliance of the Commonwealth of Kentucky with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2003. Several agencies were audited for compliance requirements in accordance with OMB Circular A-133 by other auditors, whose reports thereon have been furnished to us, and our opinion presented herein, insofar as it relates to these agencies listed in Appendix 1 to this report, is based on the reports of the other auditors.

The Commonwealth's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Commonwealth's management. Our responsibility is to express an opinion on the Commonwealth's compliance based on our audit.

The Commonwealth's basic financial statements included the operations of the state universities, which expended \$539,420,974 in federal awards that are not included in the schedule of expenditures of federal awards for the year ended June 30, 2003. The expenditures for Eastern Kentucky University and Kentucky State University were not available and no expenditures relating to them have been included in the above amount. Our audit, described below, did not include the operations of the state universities because they engaged other auditors to perform an audit in accordance with OMB Circular A-133.

Report on Compliance With Requirements Applicable to Each  
Major Program and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133 and on the  
Schedule of Expenditures of Federal Awards  
(Continued)

Except as discussed in the following paragraph, we conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Commonwealth's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Commonwealth's compliance with those requirements.

We were unable to obtain sufficient documentation supporting the compliance of the Commonwealth with CFDA 21.999, Jobs and Growth Tax Relief Reconciliation Act regarding activities allowed/unallowed and allowable costs/cost principles, nor were we able to satisfy ourselves as to the Commonwealth's compliance with those requirements by other auditing procedures.

In our opinion, based on our audit and the reports of other auditors, except for the effects of such noncompliance, if any, as might have been determined had we been able to examine sufficient evidence regarding the Commonwealth's compliance with the requirements of CFDA 21.999, Jobs and Growth Tax Relief Reconciliation Act regarding activities allowed/unallowed and allowable costs/cost principles, the Commonwealth complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2003. The results of our auditing procedures also disclosed other instances of noncompliance with requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 03-CFC6-28, 03-CFC7-29, 03-CFC8-30, 03-CFC10-31, 03-JUST1-32, 03-JUST2-33, 03-JUST3-34, 03-JUST4-35, 03-JUST5-36, 03-MIL2-37, 03-TC11-38, 03-CWD10-40, and 03-CWD11-41.

Report on Compliance With Requirements Applicable to Each  
Major Program and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133 and on the  
Schedule of Expenditures of Federal Awards  
(Continued)

Internal Control Over Compliance

The management of the Commonwealth is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Commonwealth's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Commonwealth's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 03-CFC7-29, 03-CFC8-30, 03-FAC8-10, 03-JUST1-32, 03-JUST2-33, 03-JUST3-34, 03-JUST4-35, 03-JUST5-36, 03-MIL2-37, 03-TC11-38, and 03-TC12-39.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness. We also noted other matters involving internal control over compliance which we have communicated to management.

Report on Compliance With Requirements Applicable to Each  
Major Program and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133 and on the  
Schedule of Expenditures of Federal Awards  
(Continued)

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth as of and for the year ended June 30, 2003, and have issued our report thereon dated December 23, 2003. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the Commonwealth's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements taken as a whole.

Several schedules of expenditures of federal awards were audited by other auditors, whose reports thereon have been furnished to us, and our opinion presented herein, insofar as it relates to these agencies listed in Appendix 1 to this report, is based on the reports of the other auditors.

The basic financial statements of the Commonwealth are prepared on an accrual/modified accrual basis of accounting. However, the schedule of expenditures of federal awards of the Commonwealth is prepared on the basis of cash disbursements as modified by the application of KRS 45.229. Consequently, certain expenditures are recorded in the accounts only when cash is disbursed. Accordingly, the schedule of expenditures of federal awards is not intended to present the expenditures of federal awards in conformity with accounting principles generally accepted in the United States of America. Also, we were unable to obtain sufficient documentation supporting the expenditures of the Commonwealth regarding CFDA 21.999, Jobs and Growth Tax Relief Reconciliation Act.

In our opinion, based on our audit and the reports of other auditors, except for the effect of the application of a different basis of accounting as explained above and the effects of such noncompliance, if any, as might have been determined had we been able to examine sufficient evidence regarding the Commonwealth's expenditures for CFDA 21.999, Jobs and Growth Tax Relief Reconciliation Act, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the Commonwealth's basic financial statements taken as a whole.



Report on Compliance With Requirements Applicable to Each  
Major Program and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133 and on the  
Schedule of Expenditures of Federal Awards  
(Continued)

This report is intended solely for the information and use of management, members of the legislature, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen  
Auditor of Public Accounts

Schedule of Expenditures of Federal Awards  
December 23, 2003

March 8, 2004

## **SCHEDULE OF FINDINGS AND QUESTIONED COSTS**

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003**

**SECTION 1 – SUMMARY OF AUDITOR’S RESULTS**

**Financial Statements**

Financial Statements: We issued an unqualified opinion on the basic financial statements of the Commonwealth for the year ended June 30, 2003.

Compliance: In relation to the audit of the basic financial statements of the Commonwealth, and the Schedule of Expenditures of Federal Awards, the results of our tests disclosed one (1) instance of noncompliance that is required to be reported under *Government Auditing Standards*. We believe the instance of noncompliance is not material.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Finance and Administration Cabinet (03-FAC2-4)	1	

Internal Control Over Financial Reporting: Our consideration of the Commonwealth’s internal control over financial reporting disclosed 27 reportable conditions. We believe none of the reportable conditions are material weaknesses.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Families and Children (03-CFC1-1, 03-CFC2-2)	2	
Finance and Administration Cabinet (03-FAC1-3, 03-FAC2-4, 03-FAC3-5, 03-FAC4-6, 03-FAC5-7, 03-FAC6-8, 03-FAC7-9, 03-FAC8-10)	8	
Cabinet for Health Services (03-CHS1-11, 03-CHS2-12)	2	
Revenue Cabinet (03-REV1-13, 03-REV2-14, 03-REV3-15, 03-REV4-16, 03-REV5-17)	5	
Transportation Cabinet (03-TC1-18, 03-TC2-19, 03-TC3-20, 03-TC4-21, 03-TC5-22, 03-TC6-23, 03-TC8-24)	7	
Cabinet for Workforce Development (03-CWD1-25, 03-CWD2-26, 03-CWD3-27)	3	

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)**

**Federal Awards and Schedule of Expenditures of Federal Awards**

Compliance: We issued an unqualified opinion on the Commonwealth’s compliance with the requirements applicable to each of its major federal programs, except for 21.999, Jobs and Growth Tax Relief Reconciliation Act, which was disclaimed. The results of our auditing procedures disclosed 13 instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133. We believe none of the instances of noncompliance are material.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Families and Children (03-CFC6-28, 03-CFC7-29, 03-CFC8-30, 03-CFC10-31)	4	
Justice Cabinet-Office of the Secretary (03-JUST1-32, 03-JUST2-33, 03-JUST3-34, 03-JUST4-35, 03-JUST5-36)	5	
Department of Military Affairs (03-MIL2-37)	1	
Transportation Cabinet (03-TC11-38)	1	
Cabinet for Workforce Development (03-CWD10-40, 03-CWD11-41)	2	

Internal Control Over Compliance: Our consideration of the Commonwealth’s internal control over compliance disclosed 11 reportable conditions. We believe that none of the reportable conditions are material weaknesses.

<u>STATE ORGANIZATION</u>	<u>REPORTABLE</u>	<u>MATERIAL</u>
Cabinet for Families and Children (03-CFC7-29, 03-CFC8-30)	2	
Finance and Administration Cabinet (03-FAC8-10)	1	
Justice Cabinet-Office of the Secretary (03-JUST1-32, 03-JUST2-33, 03-JUST3-34, 03-JUST4-35, 03-JUST5-36)	5	
Department of Military Affairs (03-MIL2-37)	1	
Transportation Cabinet (03-TC11-38, 03-TC12-39)	2	

**COMMONWEALTH OF KENTUCKY  
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FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)**

**Federal Awards and Schedule of Expenditures of Federal Awards**

Schedule of Expenditures of Federal Awards: We issued a qualified opinion on the Commonwealth’s Schedule of Expenditures of Federal Awards because of the effect of the application of a different basis of accounting that is not in conformity with accounting principles generally accepted in the United States of America as described in Note 1 of the schedule and the effect of the scope limitation relating to CFDA 21.999, Jobs and Growth Tax Relief Reconciliation Act. The opinion was issued in relation to the basic financial statements of the Commonwealth taken as a whole.

**Identification of Major Programs**

The following is a list of major Type A programs:

<b>CFDA #</b>	<b>Program Title</b>
<b>Food Stamp Cluster:</b>	
<b>10.551</b>	Food Stamps
<b>10.561</b>	State Administrative Matching Grants for Food Stamp Program
<b>Child Nutrition Cluster:</b>	
<b>10.553</b>	School Breakfast Program
<b>10.555</b>	National School Lunch Program
<b>10.556</b>	Special Milk Program for Children
<b>10.559</b>	Summer Food Service Program for Children
<b>10.558</b>	Child and Adult Care Food Program
<b>10.766</b>	Community Facilities Loans and Grants
<b>11.550</b>	Public Telecommunications Facilities – Planning and Construction
<b>14.117</b>	Mortgage Insurance-Homes
<b>14.228</b>	Community Development Block Grants/State’s Program
<b>14.239</b>	HOME Investment Partnerships Program
<b>17.225</b>	Unemployment Insurance
<b>17.255</b>	Workforce Investment Act
<b>Workforce Investment Act Cluster:</b>	
<b>17.258</b>	WIA Adult Program
<b>17.259</b>	WIA Youth Activities
<b>17.260</b>	WIA Dislocated Workers
<b>Highway Planning and Construction Cluster:</b>	
<b>20.205</b>	Highway Planning and Construction

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)**

**Identification of Major Programs (Continued)**

<b>CFDA #</b>	<b>Program Title</b>
<b>21.999</b>	Jobs and Growth Tax Relief Reconciliation Act
<b>64.114</b>	Veterans Housing-Guaranteed and Insured Loans
<b>66.458</b>	Capitalization Grants for Clean Water State Revolving Funds
<b>66.468</b>	Capitalization Grants for Drinking Water State Revolving Funds
<b>83.544</b>	Public Assistance Grants
<b>84.010</b>	Title I Grants to Local Educational Agencies
<b>Special Education Cluster:</b>	
<b>84.027</b>	Special Education-Grants to States
<b>84.173</b>	Special Education-Preschool Grants
<b>Student Financial Assistance Programs Cluster:</b>	
<b>84.032</b>	Federal Family Education Loans
<b>84.281</b>	Eisenhower Professional Development State Grants
<b>84.334</b>	Gaining Early Awareness and Readiness for Undergraduate Programs
<b>93.558</b>	Temporary Assistance for Needy Families
<b>93.563</b>	Child Support Enforcement
<b>Child Care Cluster:</b>	
<b>93.575</b>	Child Care and Development Block Grant
<b>93.596</b>	Child Care Mandatory and Matching Funds of the Child Care and Development Fund
<b>93.667</b>	Social Services Block Grant
<b>93.767</b>	State Children’s Insurance Program
<b>Medicaid Cluster:</b>	
<b>93.775</b>	State Medicaid Fraud Control Units
<b>93.777</b>	State Survey and Certification of Health Care Providers and Suppliers
<b>93.778</b>	Medical Assistance Program
<b>Disability Insurance/SSI Cluster:</b>	
<b>96.001</b>	Social Security-Disability Insurance

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 1 – SUMMARY OF AUDITOR’S RESULTS (CONTINUED)**

**Identification of Major Programs (Continued)**

The following is a list of major Type B programs:

<b>CFDA #</b>	<b>Program Title</b>
<b>16.575</b>	Crime Victim Assistance
<b>16.579</b>	Byrne Formula Grant Program
<b>16.588</b>	Violence Against Women Formula Grants
<b>84.352</b>	School Renovation Grants
<b>84.367</b>	Improving Teacher Quality State Grants
<b>93.283</b>	Centers for Disease Control and Prevention-Investigations and Technical Assistance
<b>93.659</b>	Adoption Assistance

**Dollar Threshold Used to Distinguish Between Type A and Type B Programs**

The maximum dollar threshold used to distinguish between Type A and Type B Programs was \$18 million. Certain component units and agencies audited by Certified Public Accountant (CPA) firms had lower dollar thresholds.

**Auditee Risk**

The Commonwealth did not qualify as a low-risk auditee.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

***Reportable Conditions Relating to Internal Controls and/or Reportable  
Instances of Noncompliance:***

**FINDING 03-CFC1-1: The Cabinet For Families And Children Password Policy  
Should Be Consistently Applied To All Local Area Network Servers**

State Organization: Cabinet for Families and Children

As was noted in the prior audit, password policies established on CFC's servers did not adhere to the agency password policies. During security vulnerability testing, the auditor received account related information from four (4) machines within two (2) CFC domains. This information was compared to the established agency password policy criteria. See the table below for a summary of the findings.

<b>Security Measure</b>	<b>Standard</b>	<b>Number of machines not in compliance with policy (and the expiration setting on those machines)</b>	<b>Percentage of 4 machines not in compliance with policy</b>
Maximum Age	31 days – GOT	3 - 42 days 1 - None	100%
Minimum Age	1 day – GOT	4 - None	100%
Minimum Length	5 characters – GOT	4 - None	100%
Lockout Threshold	5 attempts – GOT	4 - None	100%

Note that one (1) of these machines had also been noted as not complying with the established password policy in the prior audit report.

Passwords are an important aspect of computer security. They are the front line of protection for system access. To help ensure the security of a network, it is necessary for a strong password policy to be developed and implemented on all servers within the network in a consistent manner. If servers within a network are not sufficiently secured, the network could be compromised.

**Recommendation**

We recommend CFC review all servers within its own domains to ensure the password policy established complies with the agency policy.



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CFC1-1: The Cabinet For Families And Children Password Policy  
Should Be Consistently Applied To All Local Area Network Servers (Continued)**

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**Management's Response and Corrective Action Plan**

*CFC acknowledges the need for uniformity in Password Policy adherence. Changes have been put into effect in order to ensure proper alignment to the Cabinet for Families and Children's written password policy. These changes have been completed and include Domain Controllers, Member Servers, as well as Local Workstation Policy.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING: 03-CFC2-2: The Cabinet For Families And Children Should Ensure All User Accounts On Its Agency Machines Are Necessary**

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State Organization: Cabinet for Families and Children

During security vulnerability testing at CFC, we discovered three (3) machines with port 21 open. The auditor was able to create a File Transfer Protocol (FTP) session through this port on two (2) machines using the anonymous or guest logins. It should also be noted that these two (2) machines were reported in the prior audit report.

The auditor noted marked improvement in the area of user account security for FY 03 in that we could not glean NetBIOS account information from any of the agency's machines.

Default administrator, guest, and anonymous accounts in operating system and applications are some of the first accounts that an intruder will attempt to use. Therefore, they should be assigned strong passwords or, if possible, renamed or removed immediately after installation.

**Recommendation**

We recommend CFC ensure access is restricted to default, anonymous, or guest logons on all machines under CFC control that have FTP services running on them.

**Management's Response and Corrective Action Plan**

*PORT 21*

*Of the three (3) systems noted, two (2) are actually the same system. Both reported FTP servers have been disabled*

*In Addition:*

*Any system found to run FTP will be noted in the Cabinet's baseline or port scans. If the service is required then it is to be migrated to one (1) of the Cabinet's firewall protected environments, otherwise the service will be disabled.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC1-3: The Finance And Administration Cabinet Should Ensure Proper Classification And Categorization Of Investments In The Cash And Investment Note**

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State Organization: Finance And Administration Cabinet

The Finance and Administration Cabinet's (FAC) Comprehensive Annual Financial Report (CAFR) team prepares the Cash and Investments note (Note 5). The CAFR team uses confirmations and independent audit reports to compile summary sheets for each entity that is a part of the Commonwealth. The summary sheets for each state government entity provide cash and investment classifications and categorizations. In reviewing supporting information for each summary sheet, problems were noted in the classification and categorization of cash and investments.

**Classification**

In reviewing the summary sheets prepared by FAC, we noted some classification errors in FY 01 and 02. This year, of the nine (9) summary sheets examined, we found one (1) had securities incorrectly classified by type of investment. For example, common stocks were classified as government securities for the Kentucky Teachers' Retirement System. All classification errors were corrected by FAC upon recommendation by the APA.

Although the total cash and investments reported on the Statement of Net Assets is correct, improper classification would cause the Note 5 disclosure to not agree with the classification of cash and investments reported in the Statement of Net Assets and could cause Note 5 to mislead a user as to the liquidity and asset allocation of the Commonwealth's investment portfolio.

Good internal controls dictate that investments be classified correctly according to type.

**Categorization**

In reviewing the summary sheets prepared by FAC, we noted some categorization errors in FY 02. This year, of the nine (9) summary sheets examined, we found two (2) had uncategorized cash that was incorrectly reported as category 3. All categorization errors were corrected by FAC upon recommendation by the APA.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC1-3: The Finance And Administration Cabinet Should Ensure Proper Classification And Categorization Of Investments In The Cash And Investment Note (Continued)**

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**Categorization (Continued)**

Improper categorization could cause Note 5 cash and/or investments to be overstated/understated, which could mislead the user about the credit risk for a particular investment.

According to GASB 3 Implementation Guide, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, Question 4, there are three (3) credit risk categories used to report cash and investments information depending on “who the securities custodian is and how the securities custodian holds the security.”

The categories required for reporting are as follows:

1. The custodian is the government’s agent and is not the counterparty or the counterparty financial institution’s trust department. The custodian holds the securities in the government’s name.
2. The custodian is the counterparty financial institution’s trust department or the counterparty’s agent and the custodian holds the securities in the government’s name.
3. The custodian is the counterparty, regardless of whether it holds the securities in government’s name.

OR the custodian is the counterparty financial institution’s trust department or the counterparty’s agent and the custodian does not hold the securities in the government’s name.

If the investment is not insured or registered or if collateral or investment is not in the possession of the government, then the investment is required to be categorized in one (1) of the above categories.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC1-3: The Finance And Administration Cabinet Should Ensure Proper Classification And Categorization Of Investments In The Cash And Investment Note (Continued)**

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**Recommendation**

**Classification**

We recommend FAC establish a procedure that would provide greater assurance that investments agree by classification to independent audit reports and other supporting documentation.

**Categorization**

We recommend consistent and proper categorization of investments be done for each state government entity for Note 5, as required by GASB 3.

**Management's Response and Corrective Action Plan**

*Procedures are in place to assure proper classification and categorization of investments, yet at times mistakes are made. The Financial Reporting Team strives for consistency and accuracy in the presentation of Note 5 as required by GASB 3. We will add a procedure to have an individual review, at a minimum, the major agencies to ensure proper classification and categorization of investments.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC2-4: The Finance And Administration Cabinet Should Strive To Ensure That All Agencies Conduct Accurate And Timely Fixed Asset Inventory Counts**

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State Organization: Finance And Administration Cabinet

FAC's Division of Statewide Accounting Services requires an annual physical inventory of fixed assets by all state agencies. FAC provides a Physical Inventory Procedures Manual for conducting the annual physical inventory. This manual provides details of how to conduct the fixed assets inventory count.

We observed fixed assets inventory counts at several agencies during our FY 03 Fixed Assets audit. Two (2) agencies, Administrative Office of the Courts (AOC) and Department of Parks, had serious deficiencies with fixed assets inventory count procedures. Our audit findings and agency responses are outlined below:

**Administrative Office of the Courts**

We observed inventory counts at the AOC Fayette County, Franklin County, and Jefferson County locations. We noted that AOC personnel conducting the inventory counts did not follow the policies and procedures outlined in FAC's Physical Inventory Procedures Manual.

**Recommendation**

We recommend that AOC conduct an annual inventory count of fixed assets following the policies and procedures outlined in FAC's Physical Inventory Procedures Manual. This would include using the 5003 Fixed Assets report to record the results of the inventory observation; searching for and adding unrecorded fixed assets; verifying and correcting the tag number, description, location, serial number, agency, organization and asset type for each asset; and making every effort to locate missing items. This would also include having adequately instructed individuals conducting the inventory counts.

**Management's Response and Corrective Action Plan**

*The AOC Department of Facilities' Property Accountability Branch, through the course of its statewide inventory in compliance with audit rules and procedures, provided State Auditor personnel weekly notices of locations and dates the 5003 inventory would be conducted. State Auditor personnel were present for portions of this process in Fayette, Franklin, and Jefferson counties.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC2-4: The Finance And Administration Cabinet Should Strive To Ensure That All Agencies Conduct Accurate And Timely Fixed Asset Inventory Counts (Continued)**

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**Administrative Office of the Courts (Continued)**

**Management's Response and Corrective Action Plan (Continued)**

*During a June 19, 2003, meeting, State Auditor personnel presented their findings to AOC personnel after all but seven (7) items had been accounted for statewide. These items included an item (presumed to be a printer) purchased in 1981, a video recorder system purchased in 1984, and information technology components, which likely have been relocated to other counties or declared surplus over the past decade.*

*AOC anticipates locating most of these items upon completion of its statewide property accountability audit.*

*State Auditor personnel noted that items were not found in Jefferson County. Most items were located on the initial inspection. Further, some items were located from the Court of Justice property accountability system via telephone. Additional research by AOC personnel enabled the inventory to be successfully completed on a subsequent visit, with the exception of three of the seven items previously discussed. State Auditor personnel were not present during this visit.*

*State Auditor personnel discussed a problem with 5003 copy "ownership." They stated that State Auditor 5003 "copies" (identical to AOC copies) were used for inventory purposes by AOC personnel in Jefferson County. This statement was true. Auditor personnel in Louisville expressed a desire to split into two groups for the sake of time. AOC obliged and performed as requested. Each group used a set of 5003 documents, one group with AOC's copy, the other with the State Auditor's copy. State Auditor personnel arrived on-site in Frankfort without 5003 documents and relied on AOC copies of the document.*

*AOC continues to extend an invitation to State Auditor personnel to accompany and observe its accountability processes throughout the Commonwealth and welcomes an inspection of its inventory system.*

*AOC concurs with the goals stated in the report's "Recommendation" narrative and will strive to achieve those goals. For the next inventory of items with a purchase price of \$5,000 and above, the Court of Justice will use bar-code*

**COMMONWEALTH OF KENTUCKY  
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FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC2-4: The Finance And Administration Cabinet Should Strive To Ensure That All Agencies Conduct Accurate And Timely Fixed Asset Inventory Counts (Continued)**

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**Administrative Office of the Courts (Continued)**

**Management's Response and Corrective Action Plan (Continued)**

*reading devices for greater accuracy and accountability. AOC is conducting a statewide, 100-percent inventory that is capturing and verifying tag numbers, descriptions, locations, agency, organization, and asset type for Court of Justice property. AOC is recording data not required via the FAC report such as serial numbers, manufacturers, room numbers, floor numbers, and photographs of some items. It is anticipated that this inventory will take one year to complete.*

**Auditor's Reply**

The auditor's role in the fixed assets inventory count process is to observe agency personnel performing the count and observe whether agency personnel follow proper procedures for the count. The auditor is not an extension of the agency and does not arrive at the inventory count with the intention to help find and count the inventory. Auditors are not required to bring any documents to the inventory count; rather they are required to obtain a copy of the agency's completed inventory record upon leaving. When auditors observe agency personnel not following proper procedures, this creates an audit finding for that agency.

In addition, any inventory items "found" after the auditor has left the site cannot be verified and therefore cannot be considered found for audit purposes.

We acknowledge that the agency is attempting to implement better procedures for the next fixed assets inventory count and encourage them to continue this effort.

**Department of Parks**

We observed fixed assets inventory counts at 17 State Parks. At ten (10) of the parks, we noted a variety of control weaknesses, including that personnel conducting the inventory counts did not follow the policies and procedures outlined in FAC's Physical Inventory Procedures Manual.



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC2-4: The Finance And Administration Cabinet Should Strive To Ensure That All Agencies Conduct Accurate And Timely Fixed Asset Inventory Counts (Continued)**

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**Department of Parks (Continued)**

We also conducted a test to confirm that historical treasures were correctly entered and tracked in the MARS fixed assets inventory system. We tested 66 items and noted that six (6) items were not entered in the MARS fixed assets inventory system and six (6) additional items were incorrectly valued.

**Recommendation**

We recommend that the Department of Parks conduct an annual inventory count of fixed assets following the policies and procedures outlined in FAC's Physical Inventory Procedures Manual. This would include using the 5003 Fixed Assets report to record the results of the inventory observation; searching for and adding unrecorded fixed assets; verifying and correcting the tag number, description, location, serial number, agency, organization and asset type for each asset; and making every effort to locate missing items. This would also include having adequately instructed individuals conducting the inventory counts.

We further recommend that the Department of Parks enter all historical treasures into the MARS fixed assets inventory using the correct values as recorded in the collection of historical treasure "books" on file at the Department of Parks.

**Management's Response and Corrective Action Plan**

*The Kentucky Department of Parks intends to fully cooperate and follow the procedures that are outlined in the FAC's Physical Inventory Procedures Manual.*

*The Fixed Asset section in the Parks Department is in the process of updating and verifying the fixed assets of Parks. The department recently completed a follow up inventory and correction documents have been processed to record the results of the physical inventory. The property officer for Parks has led this effort.*

*Parks management will make sure all staff responsible for conducting the physical count in the future is aware of the procedures outlined in FAC's Procedures Manual. We will make every effort to locate and record the Parks fixed assets accurately in MARS.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC2-4: The Finance And Administration Cabinet Should Strive To Ensure That All Agencies Conduct Accurate And Timely Fixed Asset Inventory Counts (Continued)**

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Department of Parks (Continued)

**Management's Response and Corrective Action Plan (Continued)**

*The Historical Treasures and Artifact inventory is being verified. Currently, two employees, Property Officer and the Assistant Director, are comparing the historical treasure "books" with MARS. They are correcting any discrepancies that are located. Parks is also in the process of having accredited appraisals of our Historic Treasures and Artifacts as funds become available. Our intention is to have our Historic Treasures appraised over the next few years.*

*We will update our records at the completion of each independent appraisal and notify the Department of Insurance of the value of the items appraised.*

*We are in the process of conducting physical inventory of our Historic Treasures and Artifacts. After completion, the records will again be updated in MARS.*

*We appreciate the findings and view this an opportunity to correct the deficiency cited.*

Finance and Administration Cabinet

**Recommendation**

We recommend FAC strive to have all agencies follow policies and procedures outlined in the Physical Inventory Procedures Manual and to provide technical assistance whenever necessary to ensure inventory counts are conducted correctly and accurately reflect the fixed assets of the Commonwealth. We further recommend FAC conduct training and closely monitor those agencies that consistently have inventory problems from year to year.

**Management's Response and Corrective Action Plan**

*FAC has provided The Inventory Observation Procedures to the agencies through the Closing Schedule. Additionally FAC is offering classes on Inventory Observation Procedures.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC3-5: The Finance And Administration Cabinet Should Ensure All User Accounts On Its Agency Machines Are Necessary**

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State Organization: Finance And Administration Cabinet

During the security vulnerability assessment testing for machines controlled by the FAC, we found several instances where it appears unnecessary user accounts were established on machines or for applications.

To examine the information provided by NetBIOS, we limited our review to 36 machines including the Primary Domain Controller (PDC), Backup Domain Controllers (BDC), SQL servers, and NT servers. NetBIOS account information was received from 16 machines, including the PDC and nine (9) BDCs, within the FAC domain. We examined the NetBIOS information from one (1) of the BDCs to search for disabled or unused accounts. There were 1,809 accounts on the BDC. The BDC contained 84 disabled accounts, or 4.6 percent, and 13 locked out accounts, or 0.7 percent. While reviewing other FAC machines, we found the guest account on five (5) other machines that had been disabled, but not removed.

To determine possible unnecessary accounts, the auditor used the criteria that the account was over the 30-day maximum password age established by FAC policy and had never logged onto the system. The BDC had 87 accounts, or 4.8 percent, that met this criterion. Further, while examining other FAC machines, we found an additional machine that had four (4) user accounts that had not been logged onto within 30 days of being established.

The auditor attempted a remote logon to known applications using various combinations of default logon passwords. A review of all machines controlled by FAC revealed 80 machines with port 21 open and 61 machines with port 23 open.

We were able to create a FTP session through port 21 on 34 machines, or 42.5 percent, using the anonymous or guest logins. In the prior year audit, 32 of these machines were also noted with port 21 related weaknesses. In addition, Telnet sessions could be established with no login or through the anonymous or guest default logins on 35 machines, or 57.4 percent, through port 23. In the prior year audit, 34 of these same machines were noted with port 23 related weaknesses.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC3-5: The Finance And Administration Cabinet Should Ensure All User Accounts On Its Agency Machines Are Necessary (Continued)**

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Intruders often use inactive accounts to break into a network. If an account has not been used for a reasonable period of time, the account should be disabled until it is needed. This minimizes the possibility that an unauthorized user will access the account. An account should be deleted if it is not going to be reinstated. Further, default administrator, guest, and anonymous accounts in operating system and applications are some of the first accounts that an intruder will attempt to use. Therefore, they should be assigned strong passwords or, if possible, renamed or removed immediately after installation.

**Recommendation**

We recommend FAC review accounts on all its machines to determine which accounts have had no password change within the last 30 days. These accounts should be evaluated to determine if they are still valid accounts required for a business-related purpose. If not, the accounts should be disabled or deleted as appropriate. Further, FAC should ensure that all machines with FTP or Telnet services running on them restrict access to default, anonymous, or guest logons.

**Management's Response and Corrective Action Plan**

*FAC has carefully reviewed the accounts in the domain and removed several hundred obsolete accounts. Several accounts will remain disabled due to the fact they are used for Mailbox accounts for conference rooms or special email accounts that are used as a RESPOND TO account only. The accounts are not directly accessed via email, but are managed through another email account. It is impossible by design to remove the guest account from the Microsoft Windows Operating System.*

**COMMONWEALTH OF KENTUCKY  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC4-6: The Finance And Administration Cabinet Should Secure Listings Of User Names And Associated User IDs For Power Users Of The Management Administrative And Reporting System**

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State Organization: Finance And Administration Cabinet

FAC has provided a list of state employee power users for Seagate Reporting software by agency name on a public Management Administrative Reporting System (MARS) website. This listing is accessible to any Internet user through the use of common web browsers and includes sensitive User IDs for the noted users.

Seagate Reporting power users listed on this site have the authority to create, design, schedule, and view reports of financial and other sensitive information stored on the MARS data servers. User ID information and associated user names at this level by agency could also be used to identify naming conventions and determine IDs of other high profile system users. Provision of this level of security information is not consistent with FAC formal policy and procedures concerning security governing MARS data.

Further, the MARS Seagate password does not expire and users of this reporting system are not required to change passwords after a period of time. Internet users currently can obtain information about MARS Seagate Reporting users such as their name, location, and their User ID. Once a potentially unauthorized intruder knows a User ID, a password cracking software can be initiated for guessing as often as necessary to obtain unofficial access to the Commonwealth's information. In many cases, the type of information that might be provided would include sensitive information that should be properly secured. The security of the Commonwealth's financial information is ultimately the responsibility of FAC.

Sensitive personal and financial data maintained by the Commonwealth should be properly secured. These measures should include securing IDs and passwords of users capable of accessing this type of information. Consistent application of established security policy and procedures provides continuity for implementation and sets the tone of management concern for strong system security.

**Recommendation**

We recommend FAC remove the noted sensitive Seagate Reporting power user information from the general public website. If FAC sees the need to list power users for informational purposes, we suggest they either find a more secure

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC4-6: The Finance And Administration Cabinet Should Secure Listings Of User Names And Associated User IDs For Power Users Of The Management Administrative And Reporting System (Continued)**

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**Recommendation (Continued)**

solution for providing that information or limit the information provided to name and cabinet only; the User ID should not be listed. Access to Seagate Reporting user information should be treated as confidential information, and security over that information should be maintained in a manner similar to that applied to user information for other MARS related applications.

**Management's Response and Corrective Action Plan**

*The report on the Internet has already been changed by FAC and the User ID is no longer listed. Only the agency/cabinet and the name of the report designer (power user) are listed.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC5-7: The Finance And Administration Cabinet Should Develop And Implement Formal Policy And Procedures To Govern Security Of The Management Administrative And Reporting System Interface Files**

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State Organization: Finance And Administration Cabinet

FAC did not develop and implement formal policy and procedures identifying management and user responsibilities concerning security governing MARS interface files.

It is ultimately the responsibility of FAC to ensure that access to MARS interface files is reasonable. Our review for FY 03 revealed that 11 users had update access to checkwriter files, as well as authorization to request these files be processed through FAC.

During the prior FY, we noted that FAC had forwarded a letter addressing the procedures for requesting users access to each agency security lead (ASL). Additionally, FAC had performed procedures to alert ASLs on the importance of segregating the duties of updating interface files and authorizing these files to be processed. They verified each ASL's awareness of user access to interface files by providing them with a list of datasets, all users within their agency that have access to them, and the type of access provided. Each ASL was required to take responsibility for such access by returning a signed Advantage Financial Security Agreement. This agreement states that the security surrounding the datasets, for which employees have access, provide sufficient internal controls to ensure that the actions initiated through the datasets are in accordance with the objectives of the agency. However, at the time of fieldwork, FAC had not performed procedures to review the reasonableness of access to MARS interface files. We feel that incorporating such procedures into a formalized security policy will ensure procedures governing access to MARS interface files are performed on a regular basis.

Consistent application of formalized security policy and procedures provides continuity for implementation and sets the tone of management concern for strong system security. Formal policies provide a security framework used to educate management and users of their security responsibilities. To help ensure strong security and the integrity of checkwriter files, it is necessary to develop and implement a formal policy identifying management and user responsibilities concerning MARS interface files. Further, the level of system access granted to users should be restricted to only areas necessary for an employee to perform assigned job duties. Allowing users the ability to update checkwriter files and authorize their processing increases the likelihood of unauthorized processing of checkwriter data, and may compromise the integrity of data processed through MARS.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC5-7: The Finance And Administration Cabinet Should Develop And Implement Formal Policy And Procedures To Govern Security Of The Management Administrative And Reporting System Interface Files (Continued)**

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**Recommendation**

We recommend FAC develop and implement a formal policy to govern the security surrounding MARS interface files. This effort should include standardizing procedures to be implemented on a regular basis. We further recommend these procedures include steps to provide a higher level of confidence in proper segregation of duties concerning update and processing of checkwriter files.

**Management's Response and Corrective Action Plan**

*The Finance and Administration Cabinet will develop and implement a policy to govern the security on checkwriter files. Included in the policy will be steps that will be taken to ensure segregation of duties concerning the update and the processing (E-mail request) of checkwriter files.*



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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC6-8: The Finance And Administration Cabinet Should Develop And Apply Formal System Development Life Cycle Procedures For The Commonwealth's Cash And Investments Statistical Analysis System Programs**

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State Organization: Finance And Administration Cabinet

The Office of Financial Management (OFM) did not develop and implement adequate formal System Development Life Cycle (SDLC) policies and procedures governing controls for program development and modifications. In addition to the lack of policies and procedures for program modification controls noted during the prior two (2) audits, the Statistical Analysis System (SAS) system manual was not completed and formalized during FY 03. In May 2002, the programs processed to generate reports for OFM and to create Journal Voucher text files for transfer to MARS were rewritten in SAS language. Subsequent to implementing the programs, a manual documenting SAS system programs was being created but remained in draft form at the time of fieldwork for FY 02. The time period between converting the system programs to SAS and the current year's review was sufficient to ensure the SAS manual was completed. However, the manual remained incomplete and in draft form throughout FY 03. Items missing from the system manual are described below. Therefore, our comment concerning the lack of policies and procedures governing program modification controls has expanded to include the lack of system documentation, as well as additional SDLC issues identified during current year testing.

The auditor noted 592 program modifications during FY 03. Prior to the development of the SAS programs, the OFM programmer was provided access to the previous application programs, and was verbally provided the objectives the SAS programs were to accomplish. Formal program specifications were not provided. The number and significance of the modifications made during FY 03 implies that the objectives and specifications of the programs developed may not have been clearly presented to the programmer prior to or during the initial program development. Therefore, it is necessary to comment on the lack of formal and complete program specifications provided by management prior to development or major modification of the SAS programs. Specific objectives and specifications can be provided within the currently used program change request (PCR) forms or as separate attachments to the change request forms.

The SAS system manual was not updated to include several programs that were implemented during the FY and does not provide a program processing flow diagram, production procedures, or contain a complete or accurate overview for a majority of the production programs.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC6-8: The Finance And Administration Cabinet Should Develop And Apply Formal System Development Life Cycle Procedures For The Commonwealth's Cash And Investments Statistical Analysis System Programs (Continued)**

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Further, OFM created and implemented the use of a production library that was intended to control OFM programmer access to production SAS programs. However, procedures and controls were not established to ensure the intended function of that library. The program modification process, as was noted during the prior year's review, allows the OFM sole programmer to test and submit the SAS programs from the programmer's personal drive, then merely request a copy of those programs be placed into the production library for audit trail purposes. However, in one (1) case, we identified a file maintained within the production library was not the correct version generated during the actual production run.

Finally, the agency did not formally adopt or consistently apply policies and procedures to control program modifications. Prior to implementing the new SAS programs, OFM designed and implemented procedures involving a PCR form to document the need for program modifications, description of modifications, testing of modifications, and authorization to implement modifications. However, these procedures were not formalized into policy and our testing revealed 219 of 592, or 37 percent of the program modifications were not supported by a PCR. The PCRs that were examined did not provide adequate documentation of the need for the modification, the description of modifications made, and had no signatures authorizing the implementation of the modification.

Without formalized SDLC procedures, management increases the risk of developing and implementing insecure, ineffective, or inaccurate systems and the risk of unauthorized changes being placed into the production environment that have an adverse affect on system processing results. SDLC procedures require adequate program specifications be provided to a programmer prior to program development to mitigate processing errors and the need for numerous program modifications. Sufficient procedures dictate that complete and accurate system documentation be developed and maintained for all critical systems, as this information is vital to ensuring longevity of the system. Further, SDLC procedures must be consistently applied and include adequate procedures to segregate the live production environment from development and testing environments.

**Recommendation**

We recommend OFM develop, implement, and consistently apply complete, formal SDLC control procedures, including providing adequate program

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC6-8: The Finance And Administration Cabinet Should Develop And Apply Formal System Development Life Cycle Procedures For The Commonwealth's Cash And Investments Statistical Analysis System Programs (Continued)**

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**Recommendation (Continued)**

specifications and understanding of program objectives, proper completion of system documentation, control and maintenance of test and production libraries, including adequate control over the migration of program changes to production and authorization and approval of program changes. Specifically, documented SDLC policies implemented should incorporate the following items:

- The SAS system manual should be completed and updated appropriately to include a complete and accurate overview of all programs used in production. This overview should include flowcharts or diagrams and a description of the programs function.
- Detailed program specifications should be provided to the programmer prior to development or significant modification of SAS programs. These specifications should be retained for audit trail purposes.
- The policies should specifically state which personnel are authorized to provide approvals for each stage of the PCR. Once proper approval has been obtained to implement the changes, then the programmer should sign off that the requested changes were made.
- Proper authorization for program modifications should be obtained and documented prior to those changes being made, the necessity for the change should be explicitly stated, documentation as to the changes made should be descriptive, and testing of the modification should be evident. This information should be included upon or attached to the PCRs.
- Testing facilities should be maintained separate from the production environment.
- A PCR should be on file for any modification where a blanket request is not acceptable. A blanket request will be accepted for modifications considered to be minor recurring maintenance. Recurring maintenance could include entering necessary parameters such as cycle number, fiscal year, date, number of days in the month, and file name changes where the file name contains a

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**FINDING 03-FAC6-8: The Finance And Administration Cabinet Should Develop And Apply Formal System Development Life Cycle Procedures For The Commonwealth's Cash And Investments Statistical Analysis System Programs (Continued)**

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**Recommendation (Continued)**

date or month that corresponds to the date/month being processed. A blanket request would also be acceptable for changes when there is a change in the referenced directory that will increase the security of production programs and data files.

- All versions of the SAS programs and data files used for or generated by daily and monthly processing should be retained for historical purposes for an established period of time.

**Management's Response and Corrective Action Plan**

*The SAS system manual is in the process of being completed and will be submitted in draft form to the APA by January 15, 2004.*

*The program has been in production long enough that the development-phase has past. There should not be any significant modifications going forward. If significant changes are made, proper documentation will be in-place before the modification goes into production.*

*A PCR has been developed and is in use. It is the goal of OFM to have a program change request for any change in the program. Discussions have taken place within OFM to ensure that all staff members understand the importance of full documentation and approval before any modifications are placed in production. We think that FY04 the APA will find we are in compliance.*

*Testing facilities are now maintained separately from the production environment. Programming duties and the administering of production programs have now been separated. Efforts are ongoing to ensure proper segregation of duties.*

*OFM has established a library that retains all current and former production programs. OFM's programmer does not have access to these programs nor to MARS or CAMRA. OFM's programmer can no longer run production programs.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC6-8: The Finance And Administration Cabinet Should Develop And Apply Formal System Development Life Cycle Procedures For The Commonwealth's Cash And Investments Statistical Analysis System Programs (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*The Office of Financial Management agrees in a large part with the findings of the Auditor of Public Accounts. OFM continues to strive to ensure that all programming is accurate and the Commonwealth's assets are properly protected.*

**COMMONWEALTH OF KENTUCKY  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC7-9: The Office Of Financial Management Should Improve Segregation Of Duty Controls**

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State Organization: Finance And Administration Cabinet

As noted in the previous audit, OFM did not employ proper segregation of duties between programmer, operator, and librarian functions. During FY 02, SAS programs were implemented to replace a number of EXCEL and ACCESS applications that accounted for and reported the Commonwealth's cash and investments for OFM. At this time, the OFM programmer employed to develop and maintain SAS programs was provided access to SAS production programs and data. Since the prior year's review, OFM has created a SAS production library, designated a librarian to move production programs to the library, and automated the compilation of daily MARS files as recommended in the audit comment from the previous year. However, OFM did not properly use the SAS production library created, and the programmer continues to have full access to production programs and data. Further, the current year's review revealed the programmer has access to additional applications and data critical to the processing of the Commonwealth's cash and investments. We identified the following control weaknesses:

- The SAS program code that processes cash and investment financial data monthly requires the programmer to manually enter critical accounting data directly into the program. The data consists of calculated amounts, such as payoff balances, adjustment amounts for each investment pool, and security lending balances for the month. All values are assigned to macro variables used throughout the program. Available supporting documentation was not sufficient to substantiate the data entered. The documentation did not provide evidence of review; detail of the calculations where applicable; and, in most instances, supervisory authorization.
- Programs in development or testing are not controlled or segregated from the programs that are in production. Movement of production files and programs to the production library is at the discretion of the programmer. Files and programs are not currently moved into the production library until after the SAS production run is complete.
- Test and production programs and data files are maintained on the programmer's personal network drive. Hence, the programmer has full access to the directory housing this information. Currently, production output is written and saved to the programmer's personal drive(s).

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC7-9: The Office Of Financial Management Should Improve Segregation Of Duty Controls (Continued)**

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- The programmer also functions as the operator for these programs, submitting the production programs for processing on a routine basis.
- The programmer manually modified the production version of the Journal Voucher text file prior to its upload to MARS for the July 2002 distribution. The documentation provided in support for this modification did not reflect evidence of supervisory review or authorization.
- The programmer has full access to the Complete Asset Management, Reporting, and Accounting System (CAMRA) that stores the critical investments data used by SAS to create the Journal Voucher to distribute monthly investment earnings.
- The programmer has enter, correct, and delete access and first level of approval to major documents and tables within MARS. The SAS generated journal voucher that distributes investment earnings monthly is recorded in MARS.

Employing strong segregation of duty controls decreases the opportunity for unauthorized modification to files and programs and the likelihood of errors or losses occurring from incorrect use of data, programs, and other resources. Programmer duties should not include the input of accounting data, discretionary migration of programs into production libraries, or performing operator procedures, such as executing production programs. Programmers should be restricted from the production environment and their activities should be conducted solely on “test” data. Programmers should not have access to the production environment. This control should be designed to ensure an independent and objective testing environment without jeopardizing the integrity of production data.

Computer operators should not have direct access to program source code. The function of this control is to ensure the computer operator does not intentionally or unintentionally introduce unauthorized or malicious source code into production. Smaller organizations that cannot easily segregate programmer duties from computer operator duties should implement compensatory controls to supervise programmer activities to ensure only properly tested and authorized programs are migrated into production.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC7-9: The Office Of Financial Management Should Improve Segregation Of Duty Controls (Continued)**

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**Recommendation**

We recommend OFM take the necessary actions to discontinue the processes that allow programmer access to production programs and data. OFM should also eliminate procedures requiring the programmer to input accounting information into production programs. OFM should take the following actions to employ proper segregation of duty controls:

- Request modification of the program code that performs month-end processing to eliminate the need for the programmer to manually enter accounting data. The programs should be developed to call in text or other input files generated by accounting personnel.
- Ensure SAS programs are properly tested prior to migrating them to production to ensure the integrity of the programs.
- Ensure the production library is used to house only the proper versions of production programs and data and that programs affecting production are run only from that library. Discontinue the process of allowing the programmer to run programs affecting production from his personal library. This may require implementing an application or modifying the programs to include security that will force the program to write to the production library without the operator or programmer having edit, update, or delete access to the library.
- Designate a computer operator other than the programmer to execute the production programs. Also, implement access controls to ensure the operator can only read and execute programs in the production environment.
- Ensure controls are implemented to maintain an audit trail for identifying applicable production programs used during the year for the period suitable for audit purposes.
- Eliminate the programmer's full access to CAMRA. If a situation occurs requiring the programmer to access CAMRA, the programmer's access should be set to 'read' or 'reporting' at the maximum as appropriate.
- Eliminate the programmer's enter, correct, delete access, and first level of approval authority to MARS documents and tables.



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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC7-9: The Office Of Financial Management Should Improve Segregation Of Duty Controls (Continued)**

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**Recommendation (Continued)**

Circumstances of an emergency nature requiring the programmer to have update access privileges should be granted only for the time period required to address the situation and must be documented and closely monitored at the appropriate supervisory level. For these circumstances a log should be created that specifically documents the individual accessing the production library by user ID, time of entry, specific programs and data accessed, and purpose and the time access was deleted. All activity should be subject to supervisory control, and system log entries should be substantiated by a formal request for the access granted.

**Management's Response and Corrective Action Plan**

*Action has been taken to eliminate the programmer's access to production programs and data. The program operator is separate from the programmer. Further, action is being taken that will eliminate procedures requiring the programmer to input accounting information into production programs and requiring the programmer manually enter accounting data.*

*All new programs and modifications to programs must have a program change form filled out. One of the sections on this form requires the internal auditor or some other staff member to test the modification before it is placed in production.*

*All daily production programs are housed in the Library and data is written to the History folder when programs are run daily by the operator. Monthly production programs will be handled the same way when testing is complete.*

*Any program changes made to the programs in the library will be accompanied by documentation identifying the changes. Only production programs are in the production library. Test programs are run on the programmer's PC.*

*The programmer's access to CAMRA has been set to "Reporting."*

*The programmer's access to MARS documents and tables has been changed to INQR (Inquiry) security group which allows 'view – only' access.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC8-10: The Finance And Administration Cabinet Should Track Federal Expenditures For The Jobs And Growth Tax Relief Reconciliation Act In The Management Administrative And Reporting System**

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State Organization: Finance And Administration Cabinet

In FY 03, the Finance Cabinet received \$68,720,606 for the Jobs and Growth Tax Relief Reconciliation Act (JGTRRA). Through the JGTRRA, the U. S. Treasury provided funds to states to be used for general government purposes under CFDA 21.999. In reviewing FAC's SEFA for the JGTRRA, we discovered FAC had failed to adequately track the expenditure of these funds as suggested by OMB Circular A-133 or the JGTRRA. Although the funds were deposited into the general fund, and we could confirm the receipt of the funds, there were no procedures in place to track how these funds were spent. The JGTRRA placed limits on how the funds were to be used; without some type of tracking procedure, the APA has no way of determining if allowable costs and/or allowable activities compliance requirements are appropriately met.

We are aware that FAC has received another \$68,720,606 in FY 04, which was also deposited into the general fund. Failing to properly track the funds received in FY 03 raises concerns that there are possible problems with tracking the proper use of the funds received in FY 04.

When federal funds are not individually and specifically identified, the federal fund information presented on the SEFA cannot be reconciled to MARS. Moreover, without proper tracking of federal expenditures, we are unable to determine if allowable costs and/or allowable activities compliance requirements are appropriately met.

OMB Circular A-133 requires that we determine if federal grant funds are used for allowable costs under the requirements of federal program. The JGTRRA specifies that the funds be used for essential government needs and, specifically, not for new programs.

Good internal controls dictate that receipts should be accounted for using a specific identifier to allow all related expenditures to be matched to their corresponding receipts.

**Recommendation**

We recommend FAC account for this federal grant in the same manner they account for their other federal grants. We recommend these funds be appropriated for a certain government need and assigned a specific identifier in MARS.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-FAC8-10: The Finance And Administration Cabinet Should Track Federal Expenditures For The Jobs And Growth Tax Relief Reconciliation Act In The Management Administrative And Reporting System (Continued)**

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**Management's Response and Corrective Action Plan**

*We agree that depositing the Jobs and Growth Tax Relief Reconciliation Act (JGTRRA) funds in the General Fund makes it difficult to track expenditures to a specific program. We were, to the best of our judgment, in compliance with the guidelines provided by the US Department of Treasury. In our application for funding we certified that the JGTRRA funds would be used to "provide essential government services for types of expenditures permitted in the most recently approved budget". We did not track expenditures to a specific program in fiscal year 2003. We plan to implement your recommendation in fiscal year 2004 and allot the JGTRRA funds to a specific program and track expenditures at the program level.*

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(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CHS1-11: The Vital Statistics Branch Should Improve Controls Over Assets And Separate Work Tasks**

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State Organization: Cabinet for Health Services

The Vital Statistics Branch issues birth, death, marriage, and divorce certificates. They collect receipts of checks and cash by walk-in and mail. We visited the agency on several occasions and noticed the following control weakness:

The Accountant III position has many duties related to receipts processing. The Vital Statistics Branch runs reports at the end of each day detailing the activity related to each cash receipts clerk. The Accountant III reviews all of these daily reports for errors. In addition to the end-of-the-day review, the Accountant III prepares the daily reconciliation and deposit.

Even though the receipts processing described above is better than the situation last year, more improvement is needed. When a separate person does not reconcile the deposits back to the daily cash receipts records, the person preparing the deposits can perpetrate a fraud with minimal risk of being detected.

**Recommendation**

We recommend the Vital Statistics Branch request the Financial Management and Reporting Branch perform a monthly comparison of the Vital Statistics receipts submitted for deposit to the original receipts accounting records. The person performing the reconciliation should be independent of the cash handling function and the original receipts accounting function.

**Management's Response and Corrective Action Plan**

*A comparison process has been implemented as recommended.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CHS2-12: The Vital Statistics Branch Should Take Appropriate Steps To Reduce Identity Theft Risks**

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State Organization: Cabinet for Health Services

The Vital Statistics Branch collects and registers data relating to Kentucky births, deaths, marriages, adoptions, and divorces. Kentucky birth and death certificates are easy to obtain and could be used for fraudulent purposes, such as identity theft. Identity theft could be facilitated since vital records can be easily obtained.

Proper internal control dictates the Vital Statistics Branch not release:

- Data which is excluded by law and
- Data which could easily facilitate identity theft or other crimes.

Kentucky is one (1) of 13 states with “open” birth records and one (1) of 19 states with “open” death records. These open records states are far less restrictive on which records are exempted from disclosure and inspection.

This comment has been presented in the last two (2) audit reports. CHS management has agreed with APA auditors that the risks noted continue to exist and need to be fixed. CHS is continuing to seek legislation to correct the problem and anticipate that the legislation will pass during the 2004 legislative session.

**Recommendation**

We recommend the branch:

- Promulgate administrative regulations as required by KRS 213.131(1) to provide adequate standards of security and confidentiality of vital records.
- Take appropriate steps, including requesting legislation, to exclude this data from potential misuse by persons seeking to commit identity theft or other unlawful acts. The end result should exclude any data that has the potential to be misused by persons seeking to commit identity theft or other unlawful acts.
- Seek to exclude social security numbers from death certificates subject to inspection under the Open Records law. The social security number on a death certificate released to the public should be excluded until such time as identity theft no longer appears to be a substantial risk.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CHS2-12: The Vital Statistics Branch Should Take Appropriate Steps  
To Reduce Identity Theft Risks (Continued)**

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**Management's Response and Corrective Action Plan**

*This item should be closed. The Department for Public Health (DPH) will continue to advocate for closed records (restrict records) if legislation is reintroduced in 2004. At present the release of information contained in vital records is not accomplished under an Open Records law. Rather, DPH remains in compliance with KRS 213.131 Inspection of Records – Public Records, as paragraph (1) reads “ To protect the integrity of vital records, to ensure their proper use, and to ensure the efficient and proper administration of the system of vital statistics, it shall be unlawful for any person to permit inspection of, or to disclose information contained in vital records or to copy or issue a copy of all or part of any record except as authorized in this chapter, by regulation, or by order of a court of competent jurisdiction.” The DPH also remains in compliance with KRS 213.136 (1), which states, “The state registrar shall upon receipt of an application issue a certified copy of a vital record in the registrar’s custody or a part thereof to any applicant.” It should be noted that this law clearly states, “The state registrar shall ...upon receipt of an application issue a certified copy...to any applicant” and that the Chapter does not allow for that requirement to be regulated or mitigated. Lastly, the DPH further maintains compliance with other protections as applicable in the Health Insurance Portability and Accountability Act (HIPAA).*

**Auditor's Reply**

The risk of identity theft continues to exist. The risk is not eliminated by the cabinet or agency legal interpretation. If legislation is needed to address the risk, then CHS should aggressively pursue obtaining such legislation. This audit risk continues to be an open audit issue, which we believe CHS management should want to close. When this audit issue is appropriately addressed, it will be closed.

**COMMONWEALTH OF KENTUCKY  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV1-13: The Kentucky Revenue Cabinet Should Improve Communication Between Divisions To Ensure Taxpayer Information Is Protected**

State Organization: Kentucky Revenue Cabinet

During the Revenue Cabinet audit, we noted problems in the refunds, accounts receivable, and receipts audit sections related to missing or difficult to locate tax returns. While searching for returns, we noted problems with the communication between the tax divisions and central files regarding tracking of tax returns transferred to central files.

**REFUNDS AUDIT SECTION**

We tested controls over refunds and noted weaknesses in Revenue's ability to retain and locate corporate tax returns to comply with confidentiality and record retention laws.

We tested 42 corporate tax refunds, and Revenue failed to provide a tax return for one (1) corporate taxpayer of \$381,004. Initially, 12 tax returns were missing, but Revenue located 11 of the returns over a one-month period. We were able to view the last return on Revenue's corporate coding system; however, we were not able to determine if the return was reviewed.

**ACCOUNTS RECEIVABLE AUDIT SECTION**

We were unable to locate one (1) corporate license tax return. The return amount due per the Compliance and Receivable System was \$440,909.

**RECEIPTS AUDIT SECTION**

We were unable to locate three (3) Motor Fuels Dealer Reports. The return amount paid per MIXERS was \$32,156.

When tax returns are missing, we cannot determine if the returns were lost, stolen, destroyed, or ever received. Thus, missing documentation causes us to question the legitimacy of a transaction, particularly when a refund is issued. Tax returns are the most persuasive evidence available to support that refunds are legitimate, properly recorded, and classified within the financial statements.

A disorganized filing system compromises Revenue's ability to properly safeguard taxpayer information, as required by KRS 131.081 and 131.185. The benefits of retaining tax records are lost, if the documentation cannot be easily located and retrieved at the central filing repository.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV1-13: The Kentucky Revenue Cabinet Should Improve Communication Between Divisions To Ensure Taxpayer Information Is Protected (Continued)**

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KRS 131.081 (15) states, “Taxpayers shall have the right to privacy with regard to the information provided on their Kentucky tax returns and reports, including any attached information or documents...no information pertaining to the returns, reports, or the affairs of a person’s business shall be divulged by the cabinet to any person . . .”

KRS 131.185 states, “Income tax returns shall be kept for five (5) years; primary accounting records of tax payments, seven (7) years; and records containing all data of motor vehicle registration, three (3) years . . .”

Good internal controls dictate tax returns be maintained in a manner that ensures compliance with confidentiality and record retention laws and ensures accountability to Kentucky taxpayers.

**Recommendation**

Revenue should ensure confidential taxpayer information is protected and preserved as required by statute. Revenue should consider improving communication between the tax divisions and the central files division. For example, one person from each division could keep track of the batches of tax returns being shipped to central files. Also, when searching for a return, the appropriate division should be notified that the return is not at central files, and a division employee should follow up with central files employees to make sure the return is located.

**Management’s Response and Corrective Action Plan**

*Revenue agrees with the auditor’s findings that additional controls should be implemented to ensure that confidential taxpayer information is protected and preserved, as required by statute.*

*As a result, Revenue has designated the Central Files Section as a restricted area, which requires an employee to have special permission in order to gain access.*

*The Division of Revenue Operations has already implemented tracking logs to document where a return was sent after processing. Similar tracking logs will also be implemented for each division to improve communication between the divisions and the Central Files Section.*



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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV1-13: The Kentucky Revenue Cabinet Should Improve Communication Between Divisions To Ensure Taxpayer Information Is Protected (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Additionally, Revenue has allocated four (4) interim resources to the Central Files Section to assist in eliminating backlogs, and to help with the purging of records that have met the required retention period.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 02-REV2-14: The Kentucky Revenue Cabinet Should Update Its Computer Systems To Remove System Limitations Affecting Accuracy And Reliability Of Reporting**

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State Organization: Kentucky Revenue Cabinet

We identified and tested 13 accelerated sales tax receipts totaling \$211,488,106. We noted the Revenue sales tax database does not process payments that equal or exceed \$1,000,000; thus, a single transaction exceeding \$1,000,000 will show up on the Revenue mainframe report as 999,999 in a succession of lines with the bottom line total as the balancing amount. Data that is processed in this manner is difficult for end users to understand.

In FY 01, this system limitation resulted in two (2) accelerated payments, which overstated receipts in Revenue's mainframe system by \$7.5 million. While no errors were found in testing this FY, the recording process that caused the errors in FY 01 has not been corrected and has the potential to cause revenues to be incorrectly recorded in the future.

While FY 03 financial statement information was not affected as a result of these weaknesses, the system limitations could affect the accuracy and reliability of the Revenue reporting system. Tax information that is not captured exactly as reported on the tax return makes it difficult to determine that receipts were recorded at the proper amounts and increases the likelihood that errors will go undetected by Revenue.

Good internal controls dictate that receipts should be properly posted to computer records from supporting documentation, and all data processed by significant systems should be reviewed to determine accuracy and completeness.

**Recommendation**

We recommend Revenue take the following actions to correct these weaknesses:

- Update the Revenue mainframe system to process tax payments that equal or exceed \$1,000,000; and,
- Complete update of Modernized Front End (MFE) to process all accelerated sales tax returns; this would reduce manual processing and should increase mathematical accuracy, which would increase the reliability of the mainframe data. If this is not feasible, due to the magnitude of the tax payments involved, all accelerated sales tax returns should have a secondary level of review that includes verifying, editing and approving all adjustments.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 02-REV2-14: The Kentucky Revenue Cabinet Should Update Its Computer Systems To Remove System Limitations Affecting Accuracy And Reliability Of Reporting (Continued)**

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**Management's Response and Corrective Action Plan**

*Revenue agrees that updating the mainframe system to accommodate payment transactions greater than \$1,000,000 would provide more concise, accurate, and efficient information for end users to interpret and understand. While the current system may be more difficult to interpret and understand, payments transactions are represented in their entirety. In addition, as noted in this audit comment, no errors were identified while testing the system for FY 2003. Given the current budget constraints and plans to build a new system for compliance to the national Streamline Sales Tax initiative, updating the current mainframe system at this time may not be a priority or the best use of resources.*

*Revenue also agrees that putting Accelerated Sales Tax returns on the MFE would be a more efficient and effective processing tool than the current environment. However, given the current budget constraints, plans for a new national Streamline Sales Tax initiative, a system rewrite, and possible legislative changes, this change will not likely occur during FY '04.*

*It is recognized that whenever a dollar amount exceeding a single payment of over \$1,000,000 is received, the Sales and Use Tax system does not display that record as one transaction. The Sales and Use Tax system does, however, contain the correct amount and this information is reflected in receipts. It is also recognized that the Sales and Use Tax system does not always effectively handle accelerated payments. These payments are worked manually by Revenue employees. It has been determined that the most effective approach is to build controls within the new Sales and Use Tax system, which is being designed to accommodate the needs of the national Streamline Sales Tax Agreement. This new system will most likely be complete within FYE [Fiscal Year End] 06.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV3-15: The Revenue Cabinet Should Strengthen The Security Surrounding Administrator Accounts**

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State Organization: Kentucky Revenue Cabinet

During the security vulnerability testing of Revenue machines, the auditor found several instances of lax security over administrator accounts, resulting in potential intrusion vulnerabilities. These instances vary in severity; combined, they demonstrate that the Revenue local area network was vulnerable during the year under review.

We examined 43 Revenue machines and found three (3) machines where the administrator accounts had not been renamed or disabled. Since these accounts cannot be locked out if the account is not renamed, these machines could be vulnerable to a brute force attack. Two (2) of these machines were included in our prior year report comment for the same issue. Further, six (6) machines were noted with administrator level accounts that had been adequately renamed; however, the passwords had not been changed frequently to comply with agency password policy. The passwords on these machines had not been changed for periods ranging from 161 to 433 days. One (1) of these machines had been noted for the same issue in our prior year report comment.

The auditor also examined all Revenue controlled machines for specific applications running on port 1433 and found that two (2) of these machines allowed the auditor to gain “Master” access through SQL using a default administrator logon. This type of access will provide an unauthorized user with complete access to the application. Further, the user would be granted local system account rights to the machine on which the application resides. The auditor initiated an SQLTool on both of these machines to view the available drives on each system and view the respective directories and files. The auditor noted an electronic file of income tax transactions on one (1) of these machines, including taxpayer attributes of names, addresses, and social security numbers. Access to this confidential data was available to unauthorized users during the audit period. This issue had been resolved at the time of our follow-up assessment in October 2003. However, the vulnerability existed during portions of FY 03.

Administrator accounts are very powerful and can allow full access to the system or application. Therefore, these accounts should be scrutinized to ensure they are adequately secured. At a minimum, the passwords for these accounts should be changed from the system defaults. Further, some administrator accounts can be renamed to help obscure them from an unauthorized user’s view. Finally, all administrator passwords should be changed in compliance with established password policies.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV3-15: The Revenue Cabinet Should Strengthen The Security Surrounding Administrator Accounts (Continued)**

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**Recommendation**

We recommend that Revenue review all machines to ensure the administrator accounts have been changed from the default naming conventions and have a password established that is not a default password. This should include a review of all SQL application administrator passwords. Finally, Revenue should ensure all administrator accounts adhere to the established password policies by ensuring all administrator level passwords are changed at the established expiration interval.

**Management's Response and Corrective Action Plan**

*KRC would like to document that the vulnerabilities discovered by APA were only uncovered after gaining internal access to the KRC network. KRC has protected its network resources from external attacks through firewall technology.*

*All servers were checked to make sure that all default administrator and guest IDs have been renamed and that default passwords have been changed. All corrections were completed by December 17. The local administrator account that was found on a workstation was appropriately removed from this machine on 12/8/03.*

*KRC policy is to change the local administrator account passwords on both workstations and servers every 30 days. Our review shows that this policy has not been followed. We have readdressed this issue with our Network Administrators and the Network Support Manager will monitor to ensure this policy is being followed in the future. We are also looking into tools or scripts that would allow us to quickly change local administrative passwords throughout the domain.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV4-16: The Revenue Cabinet Should Ensure All User Accounts On Its Agency Machines Are Necessary**

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State Organization: Kentucky Revenue Cabinet

During the security vulnerability testing of Revenue machines, the auditor discovered several instances where services were established without adequate user account control.

The auditor attempted a remote logon to machines with known applications accessible through a FTP session. The auditor was able to create an FTP session through port 21 on five (5) machines with the anonymous logins. These machines allowed connections without having to provide any type of user ID or password. One (1) of these machines was a web server, and the FTP service allowed anonymous access to all directories and files on the web server. However, no sensitive tax information was viewable on this web server through this FTP service.

Intruders often use inactive accounts to break into a network. If a user account has not been utilized for some time, the account should be disabled until it is needed. This minimizes the possibility that an unauthorized user will use the account. If an account is not going to be reinstated, then it should be deleted. Further, default administrator, guest, and anonymous accounts in operating systems and applications are some of the first accounts that an intruder will attempt to use. They should be assigned strong passwords or, where possible, renamed or removed immediately after installation.

**Recommendation**

We recommend Revenue ensure all machines with FTP services running on them restrict access to default, anonymous, or guest logons as necessary.

**Management's Response and Corrective Action Plan**

*KRC would like to document that the vulnerabilities discovered by APA were only uncovered after gaining internal access to the KRC network. KRC has protected its network resources from external attacks through firewall technology.*

*Revenue staff reviewed all instances of FTP services and has ensured that only those that require it for a business need have it enabled. We have also ensured that all of these servers have anonymous access disabled. One server mentioned*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV4-16: The Revenue Cabinet Should Ensure All User Accounts On Its Agency Machines Are Necessary (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*is a server not in the Revenue domain. This server is within the GOT domain and Revenue forms are stored there for citizens to FTP from the web. It is our understanding that anonymous has been enabled on that server which is administered by GOT.*

*Revenue also reviewed machines that were running SMTP and determined that two of the four instances could be disabled. That was completed in early December.*

*Revenue has reviewed all servers currently installed and renamed administrator and guest accounts. We have restricted anonymous wherever possible.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-REV5-17: The Kentucky Revenue Cabinet Should Develop A System For Reconciling Critical Information And Investigating Any Discrepancies**

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State Organization: Kentucky Revenue Cabinet

Revenue does not have a system in place to input or reconcile critical information to the mainframe system; this has been reported during prior audits and continues to be a problem. Due to the lack of reconciliation, Revenue cannot ensure that amounts reported remitted are correct. While Revenue has had a reconciliation project underway for several years, the system was not operational during the FY 03 audit. It is expected that the project will be fully operational by the end of FY 04.

Failure to reconcile increases the chance that fraudulent reporting would go undetected by Revenue. By not reconciling this information, the Commonwealth may not be receiving the correct amount of income tax due.

Revenue should have adequate systems in place to reasonably ensure that all taxes due the Commonwealth are collected, and taxpayers are reporting key information in compliance with Commonwealth laws. Reconciling is a key component to determining taxpayer compliance and should be part of Revenue's taxpayer compliance programs.

**Recommendation**

Revenue should develop a system for reconciling critical information and investigate any discrepancies. The proposed reconciliation system will allow Revenue to perform several different types of reconciliations.

**Management's Response and Corrective Action Plan**

*The reconciliation system is now in place and one of the critical reconciliations recommended is currently being performed. In addition, the second phase of the reconciliation system, which will allow Revenue to perform other types of reconciliations, is scheduled to be completed in Fiscal Year 05.*



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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented**

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State Organization: Transportation Cabinet

The Transportation Cabinet (TC) did not provide adequate network security controls to protect critical programs and data residing on their network. Our security vulnerability assessment revealed several significant findings concerning the TC network. These findings are summarized below:

1. Critical system user account password policies were not adequately implemented or monitored. Our examination revealed the following issues concerning user account access controls.
  - Thirty-three routers/switches were identified with default or null (blank or non-existent) passwords.
  - Two (2) wireless network access points provided web-based management.
  - Enumerating gave us the encrypted password for two (2) Virtual Network Client (VNC) clients. A freeware program from the Internet cracked it in less than a second. This provides a GUI based remote control of this, and other, VNC hosts.
  - An Oracle database system was noted with a null password for its SYS account that is the controlling account for Oracle systems.
  - Over 22 host machines were identified with null passwords (the absence of a password) on the local administrator login account. Additional scanning reported ADMINISTRATOR accounts (highly privileged account used by those who maintain the network) with null passwords assigned. An administrator account was found on several host machines with a null password that had no apparent significant usage.
2. An adequate intrusion detection and response system was not implemented.
  - Our examination revealed that on April 2, 2003, a hacker “toolkit” containing specific programs was uploaded to the TC network on a proxy server. This is the same proxy server that is described below in issue number three (3). These toolkit programs can be used to enumerate sensitive information that assists an intruder to escalate their privilege and access to this and other systems. We noted that the intruder had used this toolkit to acquire the clear text password hashes (sam.txt) from this machine, including several administrative accounts that could be used to access other machines on the TC network. These password hashes are easily deciphered using utilities freely

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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available on the Internet. Further, this password hash file was available to any Internet user that might also have come across these vulnerabilities. This file was accessible, at a minimum, from April 2, 2003 until the agency was notified on July 29, 2003. Anyone who found this hash file could have gained control of the agency systems and data.

- Two (2) servers, one (1) FTP and one (1) Internet Relay Chat (IRC) were installed by the intruder and were actively used by several overseas computers. The FTP server was covertly running as the Multimedia Support Task (MMTASK) program that was established using a Firedaemon tool. The Firedaemon.exe tool is used to launch regular programs as services. This allows the program to run at all times regardless of who, if anyone, is logged onto this system whenever the computer is turned on. It also masks the program by changing its name. In this case, the service was named MMTASK, which is similar to MSTASK, a common service, in order to make this service more difficult to identify. Further review of this server revealed pirated copies of currently released movies, pirated copyrighted French medical textbooks, and DVDs and music CDs loaded on the servers that were possibly being sold as a result of the IRC sessions. The TC security administrators had not identified the presence of these files, despite the large amount of disk space they required.
3. Adequate procedures were not implemented to monitor employee Internet traffic.
- One (1) of the host machines noted in our examination with a null administrative password was identified as a proxy server. A proxy server acts as a middleman between web browsing clients and the web servers. Proxy servers are used to cache requested pages for quicker response as other clients request the same page, and monitoring/filtering the web servers' clients are permitted to visit. We examined the server logs for 24 dates between September 20, 2002 and June 10, 2003. Our examination of these logs revealed that approximately 212 machines within the TC network were used to actively access at least 22,237 pornographic images. Further review has revealed some of those images included child pornography. Although the agency policy prohibited this type of access, no procedures were established to monitor for improper Internet activity.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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Further, a referral was made to the U.S. Attorney for the Eastern District of Kentucky, the Federal Bureau of Investigations (FBI), and the State Attorney General regarding the system access of child pornography.

These security issues resulted in a lack of sufficient system controls to detect and prevent an unauthorized individual from gaining access to and possibly altering or destroying critical systems or related data housed on the TC network. Further, current system security controls were not adequate to prevent waste caused by frequent or habitual Internet access. Also, current security procedures did not ensure employee Internet access was limited to proper business content. The lack of sufficient system controls resulted in increased substantive audit work for the APA financial auditors in order for them to rely on the TC generated financial data applicable to their audit.

For general security to be effectively implemented and maintained, written policies and procedures should be developed. Formalized security policies provide continuity for policy implementation and illustrate management's concern for strong system security. Security policies should include roles and responsibilities of key positions necessary to identify and respond to a computer incident or intrusion from external or internal sources. Effective security also requires that password policies be designed, implemented, and enforced to ensure system user accounts, especially administrator level accounts, are protected by passwords that are of sufficient complexity. Failure to adequately secure the system increases the likelihood of unauthorized data or program modification, destruction of assets, and interruption of services. Finally, security measures should include procedures to monitor for inappropriate Internet activity of agency employees.

**Recommendation**

We recommend the following steps be taken by the TC to improve overall network security, to mitigate current and near-term risk, and to begin recovery from the noted system intrusion:

1. All privileged account passwords should be changed to strong passwords that resist cracking. Specifically, passwords must be improved for the Microsoft administrative accounts (local system and domain), any service that runs as the local system (backup exec for example), and all user accounts with administrative (local or domain)

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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate  
Network Level Security Procedures Are Implemented (Continued)**

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**Recommendation (Continued)**

privileges. The TC should ensure their current policy addresses the issue of password control and that those policies are adequately distributed to the TC employees.

2. The agency firewalls should be configured to block access to the unauthorized services (IRC and FTP) on the compromised host, while also logging the addresses of hosts (internal and external) attempting these connections for further investigation.
3. The compromised host should be removed from the network, after which appropriate forensic procedures and tools should be applied to capture all live data (processes, status data) disk partition information. This recommendation would apply to any other host that might subsequently be determined to have been compromised.
4. Application and data backups should be considered tainted and used for restoration only after having been validated in some way as authentic and not compromised.
5. The tools that have been planted on the compromised system are often used to further compromise the operating system and expand the intruder's unauthorized privilege and access, and to do so covertly. This requires that this system be effectively rebuilt from the original product media. This includes the operating system, all applications, all patches and upgrades, and all configurations. This applies to all other hosts that might subsequently be determined to have been compromised.
6. The forensically sound log files and other evidence found on systems that might subsequently be determined to have been compromised should be passed on to the Attorney General and U.S. Attorneys Office.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate  
Network Level Security Procedures Are Implemented (Continued)**

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**Recommendation (Continued)**

7. Procedures should be implemented to monitor and restrict inappropriate employee Internet activity. Further, once the TC reviews the audit trail concerning inappropriate web site activity, appropriate actions should be taken by the agency to ensure deterrence of similar activity in the future.

**Management's Response and Corrective Action Plan**

*We are eager to take the necessary actions to ensure the integrity of our financial and technology systems, and towards that goal we have the following to report. The responses are structured along the lines of the findings and recommendations made by the Auditor of Public Accounts; some duplication is contained within the responses to be sure that all points are adequately addressed.*

**Management Response to Findings:**

1. *Critical system user account password policies were not adequately implemented or monitored.*
  - *33 routers/switches were identified with default or null (blank or non-existent) passwords.*

*Response: We concur with the APA's identification of these devices, as they were configured and located on the infrastructure at the time of the APA report, as being a risk to the TC network. In order to mitigate this risk TC has made the necessary network modifications in order to limit the access points from which these devices can be managed. Noting the differences between ID/password and community strings, of the 33 addresses/devices supplied, 17 devices use community strings, 15 addresses exist logically on two physical devices that can have ID/passwords, and 1 device (hub) has a built-in ID but can have a password. As stated above, in order to mitigate this risk TC has made the necessary network modifications in order to limit the access points from which these devices can be managed and added/strengthened password authentication on those devices capable of such. Sometime between our original installation and implementation of the Baystack devices and your*

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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate  
Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*audit work in July 2003, a firmware update on these devices included the ability to provide for userid/password authentication; we apparently overlooked this enhancement. While we cannot attest to the exact timing of our installation of the firmware upgrades, it is likely that we made the firmware upgrade prior to your July 2003 audit work. We will implement this ability in the immediate future.*

- *Two wireless network access points provided web-based management.*

*Response: We concur with the risk identified in the APA report and have made the necessary network modifications in order to limit the access points from which these devices can be accessed.*

- *Enumerating gave us the encrypted password for two Virtual Network Client (VNC) client. A freeware program from the Internet cracked it in less than a second. This provides a GUI based remote control of this, and other, VNC hosts.*

*Response: We agree with the risk identified concerning usage of the Virtual Network Client (VNC) and have removed this remote control software. Traffic originating from this software has been blocked. Computers/users requiring remote control capabilities have been provided licenses/access to PCAnywhere.*

- *An Oracle database system was noted with a null password for its sys account that is the controlling account for Oracle systems.*

*Response: We refute the findings reported in the APA report relating to this issue. The screen-shots provided in the APA report offer no evidence that the SYS password was null or had ever been null. Furthermore, subsequent investigation performed upon receipt of the APA report, indicate that the SYS password was not null. The screen-shots did indicate however, that the WEBDB password had been compromised which, since WEBDB has DBA privileges, could have allowed the hacker to change the SYS password to anything other than null; Oracle will not accept a null password. No Oracle account (within TC) is an operating system account; we do not believe it likely that hackers were in control of*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*this Oracle machine. We do acknowledge that a hacker would have had the ability to control the Oracle database permitting them to change data if desired. Other than that possibility, we have not found any indication that a hacker has been on this Oracle database. The WEBDB password was changed to comply with the stronger password rules set by TC.*

- Over 22 host machines were identified with null passwords (the absence of a password) on the local administrator login account. Additional scanning reported ADMINISTRATOR accounts (highly privileged account used by those who maintain the network) with null passwords assigned. An administrator account was found on several host machines with a null password that had no apparent significant usage.*

*Response: We concur with the findings reported in the APA report and have taken the following corrective actions. TC with assistance and expertise provided by GOT, assessed password strength and compliance. As a result of these efforts, as well as from internal reviews, the Cabinet's password requirements were revised and significantly strengthened and now surpass the enterprise requirements. Privileged account passwords were changed to meet these new requirements on or about August 7, 2003. Since that time we have employed password-checking software to evaluate the strength of not only these privileged accounts but also all passwords. We continue to evaluate the strength of the passwords on an ongoing basis and share these findings with Cabinet management.*

- 2. An adequate intrusion detection and response system was not implemented.*
- Our examination revealed that on April 2, 2003 a hacker "toolkit" containing specific programs was uploaded to the TC network on a proxy server. This is the same proxy server that is described below in issue number three. These toolkit programs can be used to enumerate sensitive information that assists an intruder to escalate their privilege and access to this, and other systems. We noted that the intruder had used this toolkit to acquire the clear text password hashes (sam.txt) from this machine, including several administrative accounts that could be used to access other machines on the TC network. These password hashes are easily*

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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate  
Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*deciphered using utilities freely available on the Internet. Further, this password hash file was available to any Internet user that might also have come across these vulnerabilities. This file was accessible, at a minimum, from April 2, 2003 until the agency was notified on July 29, 2003. Anyone who found this hash file could have gained control of the agency systems and data.*

*Response: The compromised server was removed from service on July 30, 2003 and physically secured under the control of our Office of Inspector General and Kentucky State Police (KSP) for use in any possible future investigative efforts. An offline forensic copy of the server was made by GOT for use in forensic analysis that they performed at the request of TC. A copy of this forensic analysis was shared with the TC Office of Inspector General and they were asked to share the information with the Attorney General and the U.S. Attorney's Office at their discretion. The forensic analysis revealed that the sam.txt file that was 'cracked' was that of this host only and not the domain sam.txt file as previously indicated, which greatly reduces the likelihood of other machines or applications on the TC network being accessed via these password hashes. The Cabinet engaged KiZAN to perform extensive scanning and vulnerability analysis. KiZAN is a Microsoft Certified Partner and won a contract award for the Commonwealth's Security Services RFP based upon their accreditation and experience. To date no evidence of further contamination within the TC infrastructure has been identified. TC in conjunction with GOT have continued to improve security in our DMZ [Demilitarized Zone] and the entire network infrastructure. The TC firewall, which at the time of the APA study was in the early stages of implementation, is now managed by GOT. Significant firewall rules have been implemented and continue to be modified in order to strengthen our network security.*

- *Two servers, one File Transfer Protocol (FTP) and one Internet Relay Chat (IRC), were installed by the intruder and were actively used by several overseas computers. The FTP server was covertly running as the MMTASK program that was established using a Firedaemon tool. The Firedaemon.exe tool is used to launch regular programs as services. This*



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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*allows the program to run at all times regardless of who, if anyone, is logged onto this system whenever the computer is turned on. It also masks the program by changing its name. In this case the service was named MMTASK, which is similar to MSTASK, a common service, in order to make this service more difficult to identify. Further review of this server revealed pirated copies of currently released movies, pirated copyrighted French medical textbooks, DVDs and music CDs loaded on the servers that were possibly being sold as a result of the IRC sessions. The TC security administrators had not identified the presence of these files despite the large amount of disk space they required.*

*Response: Presently, as part of the KIZAN engagement, we are evaluating the possible IDS [Intrusion Detection Systems] and IPS [Intrusion Prevention Systems] solutions to further strengthen our network monitoring and management. As described earlier, significant firewall rule-set hardening has been implemented in order to block illegitimate traffic. GOT was asked, and continues to monitor traffic to the TC network and makes us aware of suspected hacking or malicious activity. A SLA has been provided to GOT which defines responsibilities and expectations relating to network monitoring.*

3. *Adequate procedures were not implemented to monitor employee Internet traffic.*

*Response: While TC will not debate the adequacy of its procedures in monitoring employee use of the Internet, the proxy server identified above is one instrument used in such activities. Internal personnel investigations and disciplinary actions are seldom publicized. We do acknowledge that additional tools, supervisory oversight, and manpower are needed to prevent abuse of state resources, such as connectivity to the Internet.*

*As follow-up to the original APA report, the investigation revealed that a number of computer sites assigned to identifiable users were found to have violated existing policy prohibiting the visiting of pornographic sites. Recommendations were made to initiate personnel actions on employees who were found to have violated the Cabinet's policy. The FBI is also currently investigating possible violations of the federal child pornography statutes.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Additional information concerning TC actions concerning the inappropriate use of the Internet can be found in our response to APA's Recommendation 7 included below.*

*TC Management Responses to Recommendations:*

1. *All privileged account passwords should be changed to strong passwords...*

*Response: The Cabinet worked with GOT to assess password strength and compliance. As a result of those efforts, as well as from internal reviews, the Cabinet's password requirements were revised and significantly strengthened and now surpass the enterprise requirements. Privileged account passwords were changed to meet these new requirements on or about August 7, 2003. Since that time, we have employed password-checking software to evaluate the strength of not only these privileged accounts but also all passwords. Passwords that are less than 8 characters have been locked and require a call to our Help Desk to be reactivated, at which time we ensure the user constructs a password that meets the new requirements. We will continue to evaluate the strength of the passwords being used over the next several months, report the findings to Cabinet managers, and emphasize full compliance.*

2. *Agency firewalls should be configured to block access ... on this host ...*

*Response: As indicated in our August 5<sup>th</sup> letter, the Cabinet implemented a firewall a couple of days after your letter and removed the host from operation. Additionally, numerous access ports have been blocked to all internal hosts [at the firewall] except to needed specific equipment. The Governor's Office for Technology (GOT) has assumed responsibility for Transportation's firewall and a Service Level Agreement (SLA) has been drafted and forwarded to GOT to define responsibilities and expectations. The IP [Internet Protocol] addresses of the intruders, which we received from your office on September 25, 2003, were provided to GOT to be checked against their logs and to monitor for future unauthorized access attempts. To expand upon this effort, we have asked GOT to take extra steps on our behalf to monitor our firewall to ensure that there are no additional vulnerabilities being exploited on our infrastructure.*

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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan(Continued)**

3. Compromised hosts should be removed from the network ...

*Response: The compromised server was removed from service on July 30, 2003 and physically secured under the control of our Office of Inspector General. An offline forensic copy of the server was made by GOT and a forensic evaluation of the server was coordinated with the Governor's Office of Technology (GOT). Other servers and systems housed on our networks also underwent review for possible compromise. The compromised server was turned over to the Kentucky State Police (KSP) on August 11, 2003 for their analysis and for further action if any. To keep from jeopardizing any investigation, no initial action was taken with the GOT forensic copy. KSP returned the server in mid-November 2003. We have provided our Office of Transportation Accountability (formerly the Office of Inspector General) with the findings from the forensic analysis of the server performed by GOT, and asked that they share the information with the Attorney General and the US Attorney's Office at their discretion. The forensic dump (copy of the server) was provided to our Office of Transportation Accountability for storage, destruction or other action at their discretion. Scans of other servers were performed; no other WAREZ sites or other hacker type intrusions were found. Efforts (described later) have been made, and are continuing, to perform a more detailed analysis; if other hosts are found to be compromised, they will be removed from operation, a forensic copy made, and the appropriate authorities including the Auditor's Office notified.*

4. Application and data backups should be considered tainted ...

*Response: We have moved all backups that were taken between April and August out of our normal rotation. In the unlikely event that we should need to use one of these backups we would restore the data to a stand-alone device first and then review the files in great detail to make sure that no suspicious files were present. We do not anticipate having to do this, but we are prepared to take that action should it become necessary.*

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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan(Continued)**

*We want to do everything reasonable to ensure that all our systems are secure and accurate. Towards that end, we have been working with GOT, and KiZAN to validate the security and soundness of our networks and critical systems – including all financial systems located on our infrastructure. The Cabinet has engaged KiZAN to perform extensive scanning and vulnerability analysis. KiZAN is a Microsoft Certified Partner and won a contract award for the Commonwealth's Security Services RFP based upon their accreditation and experience. As you are probably aware, they have performed similar audit efforts for other state agencies. KiZAN has produced draft preliminary reports of our critical servers and our network infrastructure for our review; the final report should be complete in the near future. We will share with your office any pertinent information or findings coming from KiZAN's work. To date we are aware of no significant issues.*

*Various other actions including the removal of unsanctioned remote control software were performed in an attempt to increase IT security. We have met with the Finance and Administration Cabinet to ensure they were aware of our system(s) compromise, as well as with the Office of Policy and Budget and Division of Accounts. Our financial systems as well as several additional internal data files were discussed. To date, we have found no evidence that hackers accessed any financial data.*

5. *Tools planted on the compromised system ... used to expand further compromise ... requires system to be rebuilt from original media ...*

*Response: The compromised server was removed from service a couple of days after your notification (after some preparation for a retaliatory attack). The new/replacement host was rebuilt from original media. Similar actions will be taken for any other host found to be compromised.*

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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan(Continued)**

6. Forensically sound log files and other evidence ... passed on to Attorney General and U.S. Attorneys Office ...

*Response: The compromised server was removed from service on July 30, 2003 and physically secured under the control of our Office of Inspector General. An offline forensic copy of the server was made by GOT and a forensic evaluation of the server was coordinated with the Governor's Office of Technology (GOT). The compromised server was turned over to the Kentucky State Police (KSP) on August 11, 2003 for their analysis and for further action if any. To keep from jeopardizing any investigation, no initial action was taken with the GOT forensic copy. KSP returned the server in mid-November 2003. We have provided our Office of Transportation Accountability (formerly the Office of Inspector General) with the findings from the forensic analysis of the server performed by GOT, and asked that they share the information with the Attorney General and the US Attorney's Office at their discretion. The forensic dump (copy of the server) was also provided to our Office of Transportation Accountability for storage, destruction or other action at their discretion. Any other system found to be similarly compromised will be treated likewise.*

7. Procedures should be implemented to monitor and restrict inappropriate employee Internet activity ...

*Response: In addition to the IT remediation efforts noted above, we are proceeding with the investigation of the pornographic instances listed in your initial report and in subsequent notices. As indicated earlier, our Office of Inspector General is coordinating the activities surrounding the abuse of the compromised server; he is also taking the lead on investigating pornographic issues.*

*The investigation has revealed that a number of computer sites assigned to identifiable users were found to have violated existing policy prohibiting the visiting of pornographic sites. Recommendations were made to initiate personnel actions on employees who were found to have violated the Cabinet's policy. The FBI is also currently investigating possible violations of the federal child pornography statutes.*

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**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate  
Network Level Security Procedures Are Implemented (Continued)**

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**Management's Response and Corrective Action Plan(Continued)**

*Recommendations were made to the Secretary of Transportation to limit access to the Internet when unnecessary for job requirements and to set the defaults on TC computers to automatically lock after 15 minutes of nonuse. In addition it was recommended that periodic searches be conducted on the server to search for pornographic sites every 60 to 90 days, and that all TC computers access the Internet through a proxy server.*

*Additional software has been procured and is in place that helps monitor and analyze usage of computers and many of the inappropriate sites have been blocked. In addition, listings of blocked sites from other Cabinets are planned for inclusion in our blocking efforts.*

**Auditor's Reply**

Concerning the Oracle Database System (responses to findings): Tools used to test security vulnerabilities can possibly provide false positives for identified vulnerabilities despite the fact that we use multiple tools to confirm identified weaknesses. We recognize that the SYS password on the Oracle database server may not have been null. However, as the agency stated in their response we did gain sufficient control of this machine to own the WebDB account and to change the SYS password at our discretion. Since this machine was accessible to the intruders, they could have controlled this machine at any time during the period in which the intrusion went undetected. This would have provided them the opportunity to make changes to the database appearing as a valid user, making it difficult to identify any unauthorized changes. We do acknowledge that we did not note any evidence of database transaction tampering on this machine during our examination.

Concerning the sam.txt file (responses to findings): Based on information obtained, even if the forensic analysis revealed the cracked sam.txt file was a local account file, these were administrator level accounts and did work on another host. This implies that the same passwords are likely used across hosts, which actually mimics a domain. Further, we had already confirmed that other domain administrator (e.g., ITC.) accounts with blank passwords could be used to successfully log into other hosts. Therefore, we have little confidence that administrative domain access was adequately limited or protected.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC1-18: The Transportation Cabinet Should Ensure Adequate  
Network Level Security Procedures Are Implemented (Continued)**

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**Auditor's Reply (Continued)**

Regarding the TC Response to Recommendations #3: This intrusion went unnoticed for at least four (4) months, due, in part, to several stealth techniques the intruders employed. Also, further evidence suggests the intrusion could have existed longer. Several of the hacker's tools imply that the intent was to obtain access to other machines on the network. One specific tool identified is well known to hackers for its use in creating back doors to compromised systems. Further, the intention to compromise other hosts is the best explanation for the presence of many of the identified hacker tools installed on the compromised host. All but one (1) of these tools are used against the host on which they reside. One (1) tool (nc.exe) is commonly used to scan remote systems and set up backdoor breaches to allow uploading of the other tools to the freshly compromised host. Many of the tools found were intentionally hidden or camouflaged to appear as valid programs. Tools were found that automatically run as services whenever the host ran regardless of who, if anyone, was logged onto the machine. At this time we have not been presented with any evidence that would provide us confidence that further hacker intrusions did not occur.

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC2-19: The Transportation Cabinet Should Strengthen The Logical Security Controls Over The Operations Management System**

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State Organization: Transportation Cabinet

During our audit of logical access security for the Operations Management System (OMS), the auditor found controls were not adequate to deter unauthorized access to the system. First, since the inception of the OMS, logical access authorization requests have been routed to the OMS Help Desk or an OMS District Coordinator through an e-mail or phone call. These requests can be to establish a new user account, to reset a password, to reinstate the right of a user to logon, to terminate a user account, to establish an activity or equipment shortlist, or to adjust available roads. Currently, the security administrators do not consistently maintain or log these logical access request communications.

Second, when a new user account is established or a password is reset, the system does not force the user to change the password on first login. Although the security administrator requests the users change their password at the first logon, they do not review the account to ensure that this change has occurred. In a related issue, when a new account is established in the OMS, the default password for the new account is the same as the account name. Therefore, since the system does not require the default password to be changed at first logon, unless the user changes their password voluntarily, it will remain the account name until it expires after 30 days.

Adequate logical security controls are necessary to ensure that unauthorized individuals are not allowed access to a system. First, all requests for access or privileges to a system should be properly authorized, reviewed, and documented. This information should be maintained and readily available for review should there be questions concerning the provision of access rights. Second, the system should not allow default passwords to be used beyond an initial logon. These passwords are normally very rudimentary and are, therefore, highly vulnerable to exploitation. Finally, password policies should be implemented to ensure adequate complexity for system passwords.

**Recommendation**

We recommend that the agency determine a base population of valid users. The most direct way to establish this population is to require section supervisors review and validate a listing of current users including each user's available modules and access rights. Any changes necessary should be provided to the OMS Help Desk. Once all changes have been made, the supervisor will be required to provide their authentication to the revised listing. These authentications should be maintained in the OMS Help Desk.



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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC2-19: The Transportation Cabinet Should Strengthen The Logical Security Controls Over The Operations Management System (Continued)**

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**Recommendation (Continued)**

Once this base population has been established, the security administrators should be required to maintain some form of documentation to support all changes to security. We would suggest a formalized request form that would include any necessary change types. Submission of these forms in hardcopy or via e-mail from supervisors would be permissible, as long as they can be authenticated and easily accessible to the auditor for review.

Further, there should be a feature added to the functionality of the OMS that forces a password change on its initial logon. An additional security feature would be to request that the default password be changed from the account name to something that is more ambiguous. We further recommend that password settings be established, if possible, to ensure adequate password complexity is required in the future.

**Management's Response and Corrective Action Plan**

*Response: We concur that there is a need to maintain adequate documentation relating to OMS authorization and will work towards that goal as proposed in the audit recommendations. We do believe that an email request from a person authorized to make OMS requests on behalf of a particular office is sufficient documentation provided it is retained and managed in an acceptable manner. We also agree that further functionality to allow for a forced password change at initial login, a default password other than the account name, and more complex passwords is desirable. Since the OMS software is a third party software system licensed to TC by TRDI, we will explore with TRDI the possibility of them modifying their baseline software to provide these additional security features.*

**COMMONWEALTH OF KENTUCKY  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC3-20: The Transportation Cabinet Should Implement Procedures To Ensure An Accurate Conversion Of Data To New Systems**

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State Organization: Transportation Cabinet

The Department of Bridge Inspections maintains its information in two (2) separate software programs located on two (2) different servers. The authoritative source for bridge information is the National Bridge Information System (NBIS), which is housed on a mainframe computer. However, the department also maintains its own data in the Kentucky Bridge Information System (KBIS), which is in development and is housed on a Windows NT server. Per discussion with the TC management, this is only temporary, and eventually KBIS will become the authoritative source for bridge information.

This type of situation increases the possibility for errors and discrepancies.

During the process of developing and implementing a new system that is replacing a current system, procedures should be established to ensure the complete and accurate conversion of current system data to the new system.

**Recommendation**

We recommend that department management ensure KBIS implementation procedures include a procedure to perform a thorough comparison of all data in NBIS and KBIS to ensure the completeness and accuracy of data housed within the new KBIS system.

**Management's Response and Corrective Action Plan**

*The Division of Operations Bridge Inspection Section still maintains its information in two separate software programs the National Bridge Information System (NBIS) that is housed on a mainframe computer, and the Kentucky Bridge Information System (KBIS) that is housed on a Windows 2000 server. This is only being done temporarily and that eventually KBIS will become the authoritative source for bridge information. During this temporary stage, which is almost final stage, we have always been successful in making sure no errors occur. We are making sure of the completeness and accuracy of bridge inspection and inventory data during on-going collection and input activities. We are hoping by July 2004 the KBIS will be implemented, and the KBIS will be part of Kentucky Bridge Maintenance system (KYBMS) software in future so that NBIS that resides on the mainframe will no longer exist.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC4-21: The Transportation Cabinet Should Implement Procedures To Ensure The Integrity Of The Highway Information System Database**

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State Organization: Transportation Cabinet

The Highway Information System (HIS) maintains data on bridges, as well as all other public roads in the state. The information contained in the HIS database is collected and maintained by various TC divisions. The integrity of the HIS data is dependent upon both the accuracy and frequency with which the data is updated and the users interpretation. It was noted in the prior year audit that there is no time schedule for updating that data. The source of the bridge information is kept on the NBIS server. The Department of Bridge Inspections maintains this data. Per current discussion with management, we noted that it has been several months since the HIS server had downloaded the latest information from NBIS and that no new processes have been implemented to compare the data contained in the HIS server with that contained in the NBIS server.

The agency has stated this was due to a scheduled replacement of NBIS. To date, no additional procedures have been performed to ensure that HIS data has been updated from the current KBIS data. The agency does expect to upgrade HIS in the first half of 2004 to actually implement a direct link to KBIS information for HIS users and eliminate the need for KBIS downloads into HIS.

When information regarding bridges is not updated periodically, the various divisions within the TC do not have the most recent information for analysis purposes. Specifically, it is important for the Division of Planning, which uses that data in HIS, to have current and reviewed information regarding bridges.

Data integrity control procedures should be established that are adequate to ensure the integrity of the data maintained within the organization's databases. Procedures should be established to ensure that data used by management remains complete, accurate and valid during its input, update and storage. Further, data elements should be balanced periodically to the control records or master files in the case of data interfaces.

**Recommendation**

Procedures should be implemented that ensure the integrity and completeness of bridge information provided to HIS users. Until the direct link between HIS and KBIS information is completed, we recommend a current download from KBIS to HIS be performed and data be refreshed at least on a quarterly basis.

**COMMONWEALTH OF KENTUCKY  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC4-21: The Transportation Cabinet Should Implement Procedures To Ensure The Integrity Of The Highway Information System Database (Continued)**

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**Management's Response and Corrective Action Plan**

*We would like to re-emphasize that bridge data is maintained and available from the Traffic & Operations Division. KBIS is the official source file for reporting and/or analysis.*

*As stated last August, our goal is to establish a link between the KBIS and HIS systems. We are currently developing a process to download bridge information from KBIS, including the new unique bridge id, to the existing HIS system. As the HIS upgrade progresses, this download will assist us in our design and plan for a potential link, and will aid the Traffic & Operations Division with improving bridge locations.*

*Our schedule for upgrading the HIS system to Highways by Exor includes a production load of existing data for evaluation by June 30<sup>th</sup> of this year, and running in parallel with the current system until it is determined that the upgrade successfully meets the Cabinet's reporting and analysis requirements.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC5-22: The Transportation Cabinet Should Improve Data Retention Practices**

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State Organization: Transportation Cabinet

Our examinations of the data retention for information maintained within the NBIS and within the Pavement Management System (Visual/PMS) revealed that year-end downloads are not kept for these databases. Information contained in the Required Supplementary Information includes prior year data. Additionally, trend analysis often requires detailed information for prior year data that may not have been included in a separate report.

Failure to retain year-end downloads means there is no practical method to determine or test the records and their corresponding field data for prior years.

Electronic data that provides support for financials included within the annual report should be retained in a manner similar to that required for non-electronic support. This data should be retained as provided for in an approved retention schedule with the Kentucky Department of Library and Archives. Master files and electronic data that is considered necessary for an audit trail should be retained as long as necessary for audit purposes.

**Recommendation**

We recommend the TC ensure they retain year-end downloads for the NBIS and Visual/PMS databases in order to facilitate and substantiate prior year reporting, as well as to provide a detail backup that can be tested for accuracy in the event clarification is needed. If upgrades to these systems have been or will be implemented, then the TC should ensure the same considerations for data retention are included in the implementation.

**Management's Response and Corrective Action Plan**

*A Bridge Management System (BMS) and a Pavement Management System (PMS) have been selected for implementation, but these systems have not been fully implemented. The pavement management data and the Bridge Inventory data at present is stored on the mainframe with back-up of the data as per GOT's policy and procedures for backing up data. Data entered in the selected Visual BMS and PMS has a date/time and user stamp in the database. Therefore, the changes in the data can be tracked. All prior year data is available to do trends analysis. With the full implementation of these two systems in the next one to two years, the stated weakness will cease to exist.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC6-23: The Transportation Cabinet Should Improve Audit Trail Procedures For Database Actions**

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State Organization: Transportation Cabinet

Adequate audit trails were not implemented for various databases within the TC. Our examination of internal controls over infrastructure assets revealed that no reports are currently generated by the TC that show the data attribute changes, records added, and records deleted. In addition, some databases do not contain a field for when the date information was entered or a field identifying the user performing the data entry.

In order to properly track potential data entry errors or other errors in the database, it is important to know when the entry error occurred and the identity of the individual making the entry.

Without adequate audit trails, it is difficult or impossible to determine the exact timing, source, and cause of database data entry errors or unauthorized changes to records. It may also result in the inability to properly recover data in the case of some errors.

Adequate audit trails should be provided to facilitate the tracing of transaction processing and the reconciliation of disputed data. Accounting systems and database management systems should include an audit trail component that includes sufficient information, such as the terminal device or microcomputer involved, user identification codes, data field affected, and time and date entries. The TC's system development life cycle methodology should include procedures requiring that each information system development or modification project have adequate audit trails specified.

**Recommendation**

We suggest the TC consider adding fields to provide sufficient audit trails of database alterations or security violations including the date entered and entry person for all changes to the critical databases. In addition, we believe the TC should consider generating a nightly report showing all changes to the database that were made each day.

**Management's Response and Corrective Action Plan**

*During analysis of the Land & Buildings database/application, new requirements were uncovered which kept increasing the scope of the project; some of the requirements also [would have] generated policy and process changes.*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC6-23: The Transportation Cabinet Should Improve Audit Trail Procedures For Database Actions (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Effectively, because of other priorities and setbacks, the effort waned. At this time, we are making a minimum number of changes to the database and system in an effort to comply with the intent of the recommendations. These changes are expected to be complete by the end of this month.*

*Further remediation efforts and/or a possible rewrite of a lands & building inventory system need to be at the direction of the system user/owner - Division of Property and Supply Services. Likewise, further responses to issues surrounding this system should likely be coordinated through the Division of Property and Supply Services.*

**COMMONWEALTH OF KENTUCKY  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC8-24: The Transportation Cabinet Should Improve Inventory Procedures For Fleet Management**

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State Organization: Transportation Cabinet

The Division of Fleet Management (Fleet Management) does not have written policies and procedures in place for conducting an inventory of their vehicles. Fleet Management did not conduct an inventory in FY 03, nor have they conducted an inventory for the past several years.

Conducting inventory periodically helps ensure accurate fixed assets records and inventory reporting. When a periodic inventory is not performed, the risk of material inventory misstatement, fraud, and other errors is greatly increased.

KRS 45.313 states, “Each budget unit shall maintain a current inventory of equipment having an original cost of five hundred dollars (\$500) or more. The inventory shall be available for examination by the Finance and Administration Cabinet at all times.”

FAP 120-20-01

Pursuant to KRS 45.313, each budget unit shall maintain a current fixed asset record of equipment having an original cost of five hundred dollars (\$500) or more and a useful life of greater than one year. To ensure compliance with the requirement, the Finance and Administration Cabinet may conduct physical audits of fixed assets records. Agencies shall enter records in the fixed asset system for nonexpendable property that promotes financial reporting, safeguarding of assets, and adequate insurance. Expendable property should be accounted for using the statewide inventory control system or an appropriate internal method of accounting for the flow of expendable property.

**I. General Provisions Pertaining to Fixed Asset Records**

- a. A state agency shall maintain current records of physical properties and equipment and make appropriate additions and deletions to fixed asset records as property is acquired or disposed.



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(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC8-24: The Transportation Cabinet Should Improve Inventory Procedures For Fleet Management (Continued)**

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- b. The administrative head of an agency shall be responsible and accountable for the custody and safekeeping of all personal property assigned to, purchased, or otherwise acquired by the agency. Each agency head shall either serve or appoint an employee of the agency to serve as agency property officer with responsibility for both maintaining the agency's fixed asset records and taking the annual physical inventory.
- c. Each budget unit shall review its fixed asset records as of June 30 each year to ensure completeness and accuracy.

Under the General Provisions of section FAP 120-12-01, all agencies are required to conduct an annual inventory. This provision helps to ensure data integrity is maintained with respect to the inventory accounting records.

**Recommendation**

We recommend that the TC develop written inventory procedures and conduct an annual physical inventory of fleet vehicles.

**Management's Response and Corrective Action Plan**

*We agree with the need to have written procedures for maintaining the inventory. We will have written policies and procedures in place with our revised Policy and Procedure manual. It is a work in progress at this moment and will be in place by the end of the current fiscal year.*

*We take exception to the statement that an inventory has not been taken. The Division of Fleet Management has not conducted a physical hands-on inventory, but we have sought and completed several "paper" inventories. A paper inventory is where we fax, e-mail, or mail a copy of our inventory system reports showing each agency their inventory. The agency checks and makes any necessary corrections and forwards the inventory sheet back to us certifying the accuracy of the updated inventory sheets.*

*We have conducted two selective paper inventories (Fleet Management owned units) in the fall of FY03 and an extensive paper inventory of all units in the Commonwealth of Kentucky fleet during January and February of 2003 for the State Legislature.*

**COMMONWEALTH OF KENTUCKY  
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FOR THE YEAR ENDED JUNE 30, 2003  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-TC8-24: The Transportation Cabinet Should Improve Inventory Procedures For Fleet Management (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*We are planning a physical hands-on inventory of all Fleet Management owned units this year. We shall have it planned and completed by the end of FY04. We shall then attempt to complete a physical hands-on inventory or a paper inventory by the close of each Fiscal Year.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD1-25: The Division Of Unemployment Insurance Should Perform Reconciliations Of Tax Payments Received By The Kentucky Revenue Cabinet To Its Mainframe Program**

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State Organization: Cabinet for Workforce Development

We found that the Unemployment Insurance – Tax Branch had not reconciled deposits made by the KRC to the postings made in the mainframe program WFUIA42 (Program 42) on employer accounts. Furthermore, supporting documentation was not maintained to verify each deposit. No single deposit could be tied to an individual employer account to ensure that the amounts paid by the employers were actually posted to their accounts.

Unemployment Insurance employer contribution payments are received and processed through the Modernized Front End (MFE) processing by the KRC. KRC also prepares the deposit for the bank and transmits the data images from the reports and payments processed that day to the Unemployment Insurance (UI) Kentucky Electronic Workplace for Employment Services (KEWES) system to post to the employer accounts maintained on Program 42.

If employer accounts are not reconciled to the deposit to ensure proper posting, it can affect the receivable balance or deferred revenue balance.

Good internal controls should ensure all cash receipts processed via the KRC MFE process reconcile to UI agency records.

**Recommendation**

We recommend procedures be implemented to reconcile the deposits made by KRC to the postings on employer accounts on a timely basis.

**Management's Response and Corrective Action Plan**

*After four years of effort to be able to reconcile to Revenue and have supporting documentation there is now a daily verification process in place. The MFE upload file of reports and payments includes the "MFE\_batch" number on each DLN [Document Locator Number] as part of the file. The MFE\_batch is a number listed on the actual deposit to the bank. This data is loaded into a table to record the deposit number for each DLN. We also receive a daily file of the deposit information containing the MFE\_batch and the amount of the deposit. The*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD1-25: The Division Of Unemployment Insurance Should Perform Reconciliations Of Tax Payments Received By The Kentucky Revenue Cabinet To Its Mainframe Program (Continued)**

**Management's Response and Corrective Action Plan (Continued)**

*MFE\_upload record is matched with the deposit record by using the MFE\_batch number. At this point, the actual deposit date is added to the record. The "MFE\_batch" and the "deposit\_date" are now part of our Oracle tables. We can query and verify deposit records. Below is an example of one of the tables used to balance.*

<b>MFE_BATC</b>	<b>DEPOSIT_D</b>	<b>AMOUNT</b>	<b>CSH_DEB_</b>	<b>TOT DIFF</b>
177448	05-JAN-04	11,132.02	11,132.02	.00
177449	05-JAN-04	4,325.39	4,325.39	.00
177450	05-JAN-04	2,734.64	2,734.64	.00
177451	05-JAN-04	4,777.59	4,777.59	.00
177452	05-JAN-04	5,620.27	5,620.27	.00
177453	05-JAN-04	5,385.28	5,385.28	.00
177454	05-JAN-04	10,620.68	10,620.68	.00
177455	05-JAN-04	6,929.44	6,929.44	.00
177456	05-JAN-04	2,309.40	2,309.40	.00
177457	05-JAN-04	83,393.09	83,393.09	.00
177509	07-JAN-04	16,515.91	16,515.91	.00

**COMMONWEALTH OF KENTUCKY  
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FOR THE YEAR ENDED JUNE 30, 2003  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD2-26: The Division Of Unemployment Insurance Should Enhance Controls To Ensure Proper Reporting Of The Closing Package**

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State Organization: Cabinet for Workforce Development

During testing of 76 delinquent employer contribution receivables and 52 deferred revenues, we discovered 46 that had the following errors:

- Payments were received timely; however, they were not posted correctly to employer accounts or were posted to the wrong employer account on Program 42, and corrections or adjustments were not made until after June 30, 2003.
- Payments were received and not automatically applied to the outstanding balance on Program 42. This resulted in accounts receivable and accounts payable balances simultaneously for the same account at June 30, 2003.
- Wages, excess wages, and taxable wages were reported incorrectly on Program 42, which created a receivable. In some instances, journal entries were performed incorrectly or the adjustment was not posted until after June 30, 2003.
- Amended returns were posted as receivables instead of journal entries being made to correct the original return. One instance was noted where two (2) returns were posted to the same quarter for the exact same amounts.
- Receivable or deferred revenue amounts reported at June 30, 2003 were not supported on the system when testing. The agency lacked adequate supporting documentation to explain these discrepancies.
- A payment was posted as a voluntary contribution (transaction code 30) instead of being applied to the corresponding report and created an incorrect accounts receivable.
- An account was bankrupt and the case was closed January 3, 2003; however, it had not been declared uncollectible in the system.
- Two (2) instances were found where the payment had been posted to the system, creating an accounts payable balance; however, the report was never posted.

An overstatement of receivables from delinquent employer contributions and deferred revenue on the closing package forms in the amount of \$18,208,099 and \$11,329,521, respectively was reported to FAC and posted into the MARS system for financial statement reporting.

Proper internal control dictates that the agency should have a computer system in place to adequately maintain employer accounts to ensure information input into the system is accurate and reliable.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD2-26: The Division Of Unemployment Insurance Should Enhance Controls To Ensure Proper Reporting Of The Closing Package (Continued)**

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Generally Accepted Accounting Principles (GAAP) dictate that governmental funds recognize revenues in the accounting period in which they become susceptible to accrual – both measurable and available. Therefore, amounts that are available, but not otherwise measurable, should be reported as deferred revenues rather than as a revenue.

**Recommendation**

During testing this year, we noted areas of improvement from the prior year audit. However, there are several areas that still need to be addressed. Computer system and staff controls should be enhanced to ensure proper reporting of the closing package forms for financial statement purposes. Corrections to computer systems and additional system controls must be implemented to prevent the reoccurrence of errors that affect the employer accounts.

**Management's Response and Corrective Action Plan**

*We will respond to each type of error identified individually.*

- Erroneous posting of payments is one of the conditions we attempted to identify and correct in our report audit process. We are making efforts to ensure that the audit process is completed in a timely fashion so that corrections and adjustments can be completed prior to the closing package. At this time we have not identified any additional edits or process steps that would reduce this occurrence, and are focusing efforts on the timeliness and accuracy of the existing correction process. We have established an on-going training course for staff involved in the report audit process to accomplish this.*
- We have developed a computer edit to identify instances where payments that should have been automatically applied to an existing receivable in order to research the reasons for the occurrences and develop solutions. We will address human error through training, incorporating appropriate corrective action in the training initiative referenced above. Where programming "bugs" are identified, we will request that GOT correct the problem as a priority.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD2-26: The Division Of Unemployment Insurance Should Enhance Controls To Ensure Proper Reporting Of The Closing Package (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

- *We have changed the report audit process to require staff to review every instance where a receivable is created for a report, which will allow us to identify and correct these data capture errors. The finding of erroneous journal entries is being addressed through additional staff training; we are also considering greater restrictions on the staff authorized to make journal entries as a further quality control measure. The finding relating to timeliness of adjustments has been addressed in our answer to the first finding, above.*
- *Instances of either amended or duplicate reports posted to the accounting system are automatically identified in our report audit process, and as noted above we believe the solution is not additional edits but a more timely completion of the quarterly audit. We are also considering eliminating the mailing of report forms to employers who file electronically, since a primary reason for duplicate entries is employers who file both an electronic and a paper form.*
- *We are retaining the reports that document changes. During our remodeling, these reports were not retained. We have also requested programming so this documentation is retained within the program and can be queried by KEIN.*
- *This finding was limited to a single incident, and we believe it was a result of human error. The process for identifying and posting voluntary contributions as distinct from regular employer payments will be reviewed with all staff responsible for these transactions.*
- *We have implemented new delinquent account management tools as a part of our KEWES process reengineering, including a more efficient method of identifying potential uncollectible accounts. We believe this will address the timeliness issue in future.*
- *This occurs most frequently when the report is filed electronically. We are investigating a solution that would hold and match payment and report data for electronic filers in KEWES before the data are submitted to the mainframe, to more efficiently identify such instances where a payment is missing the corresponding report. Meanwhile, this condition can be identified*

**COMMONWEALTH OF KENTUCKY  
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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD2-26: The Division Of Unemployment Insurance Should Enhance Controls To Ensure Proper Reporting Of The Closing Package (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*and corrected when delinquent report assignments are issued. To the extent that we complete the report audit cycle in a more timely fashion, as discussed above, we would expect to make these assignments sooner and thus find and correct instances of missing reports.*



**COMMONWEALTH OF KENTUCKY  
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(CONTINUED)**

**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD3-27: The Cabinet For Workforce Development Should Strengthen The Security Of Administrator Accounts**

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State Organization: Cabinet for Workforce Development

Vulnerability testing of Cabinet for Workforce Development (CWD) machines revealed several instances of lax security over administrator accounts, resulting in the potential of machines being vulnerable to intrusion. These instances vary in severity, but illustrate that the CWD local area network was vulnerable during FY 03.

We examined two (2) CWD machines that provided NetBIOS information during the current year's review. Additionally, four (4) machines that have provided NetBIOS information since FY 02 were reviewed as a follow-up procedure. Administrator accounts on five (5) of the machines had not been renamed or disabled. Each machine had administrator accounts that have never been logged into. Since the administrator cannot be locked out, if the account is not renamed, the machine could be vulnerable if a potential intruder attempted to gain access by guessing the administrator password through a brute force attack.

Administrator accounts are very powerful and can allow full access to the system. Therefore, these accounts should be scrutinized to ensure they are adequately secured. At a minimum, the account passwords for these accounts should be changed from the system defaults. Further, some administrator accounts can be renamed to help obscure them from an unauthorized user's view.

**Recommendation**

We recommend that CWD review all machines to ensure that the local administrator accounts have been changed from the default naming conventions and require the use of a password. Further, all applications that might allow a user access to the system or to configuration settings should be reviewed to ensure that default logons are not allowed.

**Management's Response and Corrective Action Plan**

*We are continuing to audit our servers for accounts that are unnecessary or need to be renamed. Most of the Administrator accounts have been changed from the default name and require the use of a secured password. Additionally, by making changes to the local security policies and registry settings we will reduce or*

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**SECTION 2 – FINANCIAL STATEMENT FINDINGS**

**FINDING 03-CWD3-27: The Cabinet For Workforce Development Should Strengthen The Security Of Administrator Accounts (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*eliminate the types of responses our machines provide. We are constantly reviewing different applications that might inadvertently allow a user access to our systems or permit access to configuration settings to ensure that appropriate changes have been made to **not** allow default logons.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

***Reportable Conditions Relating to Internal Controls and/or Reportable  
Instances of Noncompliance:***

**FINDING: 03-CFC6-28: The Cabinet For Families And Children Should Require  
State Colleges, Universities, And Area Development Districts To Submit An Annual  
Audit Report**

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State Organization: Cabinet for Families and Children

Federal Program: CFDA 17.253 - Welfare-to-Work Grants to States and Localities  
CFDA 93.558 - Temporary Assistance for Needy Families  
CFDA 93.563 - Child Support Enforcement  
CFDA 93.575 - Child Care and Development Block Grant

Federal Agency: U.S. Department of Labor  
U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: None

CFC contracts with local not-for-profit organizations, community action agencies and area development districts (ADDs), universities, and county attorneys to provide services to needy families. Program deficiencies were noted regarding Welfare to Work (WtW), Child Support Enforcement (CSE), Child Care and Development Block Grant (CCDBG), and Temporary Assistance for Needy Families (TANF). As subrecipients of federal awards, organizations that expend in excess of \$300,000 are required to have a single or program-specific audit in accordance with OMB Circular A-133. The audits must be submitted to CFC for review within nine (9) months after the end of the fiscal year audited.

We tested CFC's compliance with subrecipient monitoring provisions of OMB Circular A-133 and noted CFC does not require state colleges, universities, and ADDs to submit an annual audit report as required by OMB Circular A-133. CFC is required by OMB Circular A-133 to obtain and review the audits from these subrecipients. Since other state agencies obtain and review these audits, CFC assumes they are in compliance. For example, audits of state colleges and universities are sent to and reviewed by the Kentucky Department of Education (KDE) for compliance with laws and regulations only for KDE's federal assistance programs.

The Department for Local Government (DLG) is presumably reviewing the audits of the ADDs; however, as stated above, CFC is still responsible for ensuring compliance requirements are met by obtaining and reviewing the ADD audits. We questioned management at DLG about performing OMB Circular A-133 desk reviews and they

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**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC6-28: The Cabinet For Families And Children Should Require State Colleges, Universities, And Area Development Districts To Submit An Annual Audit Report (Continued)**

indicated they have not performed this task in several years, and they currently do not have the resources to review the audits submitted by the ADDs. CFC has cited KRS 147A.004, "Distribution of state and federal planning funds," in its policies and procedures manual as a basis for not obtaining and reviewing the ADD audits. However, CFC's federal assistance contracts with the ADDs are not a distribution of funds for planning purposes.

We also noted there continues to be a problem with the turnaround time of audits sent to OIG for OMB Circular A-133 desk reviews.

Refer to the table below for the exceptions noted during the FY 03 audit:

<b>CFDA #</b>	<b>Subrecipient</b>	<b>A-133 Audit Deficiency</b>
93.575 CCDBG	Childcare Council of Kentucky	Audit for 2002 was not submitted.
93.563 CSE	Jefferson County Attorney	No desk review performed for the 2002 audit.
	Kenton County Attorney	No desk review performed for the 2002 audit.
	Pike County Attorney	Audit for 2002 was not submitted.
17.253 WtW	Bluegrass ADD	No desk review performed for the 2002 audit.
	City of Louisville	No desk review performed for the 2002 audit.
	U.K. Research Foundation	Audit for 2002 was not submitted.
93.558 TANF	Kentucky Community & Technical College System	Audit for 2002 was not submitted.
	Big Sandy ADD	No desk review performed for the 2002 audit.

Similar problems were noted during FY 98, FY 99, FY 00, FY 01, and FY 02. We maintain our position that it is ultimately CFC's responsibility to ensure subrecipients comply with the audit requirements of OMB Circular A-133 by submitting an audit report; performing timely desk reviews; and, following up on areas of concern. This is an ongoing problem and, while improvements have been made, there is still much work to be done to achieve compliance.

Without proper oversight, CFC cannot be assured that subrecipients are expending federal awards for their intended purpose and complying with the requirements of OMB Circular A-133.

**COMMONWEALTH OF KENTUCKY  
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**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC6-28: The Cabinet For Families And Children Should Require State Colleges, Universities, And Area Development Districts To Submit An Annual Audit Report (Continued)**

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OMB Circular A-133, Subpart B states: “[n]on-Federal entities that expend \$300,000 or more in a year in Federal awards shall have a single or program-specific audit conducted for that year in accordance with the provisions of this part.”

CFC has the following responsibilities under OMB Circular A-133, Subpart D (d):

- 1) Advise subrecipients of requirements imposed on them by federal laws, regulations, and provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.
- 2) Ensure required audits are performed and require subrecipients to take prompt corrective action on any audit findings; and,
- 3) Evaluate the impact of subrecipient activities on the pass-through entity’s ability to comply with applicable federal regulations.

The Commonwealth of Kentucky Master Agreement, which is the contract between CFC and CHS/OIG states that OIG will: 1) Perform reviews and audits to ensure financial compliance with state and federal laws and regulations and evaluate external audits performed for the Cabinet, and perform other related services. 2) Complete desk reviews of A-133 audits within six (6) months of receipt. 3) Meet the standard 100% of the time.

OMB Circular A-133 §\_\_\_\_.225 states,

[n]o audit costs may be charged to Federal awards when audits required by this part have not been made or have been made but not in accordance with this part. In cases of continued inability or unwillingness to have an audit conducted in accordance with this part, Federal agencies and pass-through entities shall take appropriate action using sanctions such as:

- (a) Withhold a percentage of Federal awards until the audit is completed satisfactorily;
- (b) Withhold or disallow overhead costs;
- (c) Suspend Federal awards until the audit is conducted; or
- (d) Terminate the Federal award.

**Recommendation**

We recommend CFC change its policies and procedures manual and remove the reference to KRS 147A.004.

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**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC6-28: The Cabinet For Families And Children Should Require State Colleges, Universities, And Area Development Districts To Submit An Annual Audit Report (Continued)**

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**Recommendation (Continued)**

We also recommend CFC comply with the provisions of OMB Circular A-133 that require a pass-through entity (CFC) to receive audit reports from subrecipients required to have an audit in accordance with OMB Circular A-133; issue “timely” management decisions on audit and monitoring findings; and, require subrecipients to take “timely” corrective action on deficiencies identified in audits and through subrecipient monitoring site visits.

**Management’s Response and Corrective Action Plan**

*Under the new state administration, the Cabinet for Families and Children and the Health Service Cabinet are being consolidated into one cabinet, the Cabinet for Health and Family Services (CHFS). It is anticipated that a by-product of the combined cabinets will be access to the full resources of the Office of the Inspector General (OIG). As a result, OIG might be able to perform the required desk reviews of all contracts in a timely manner. It is hoped that, when performing desk reviews, the OIG will review the multiple contracts that CHFS has with any given vendor.*

*Issue: The CHFS - Contracts Management Branch (CMB) does not require colleges and universities to submit their audits for review. Resolution: We were informed by OIG previously that these audits were included in the state audit, CAFR and SSWAK. However, CMB will require submission of colleges and universities’ audits and complete desk reviews. Note that CMB is limited with only one audit staff member and will need additional auditors if OIG cannot perform these.*

*Issue: CMB does not perform audits of area development districts (ADD). Resolution: CMB will require submission of ADD audits and complete desk reviews. Note that CMB is limited with only one audit staff member and will need additional auditors if OIG cannot perform these.*

*Issue: KRS 147A.004 pertains to planning funds and recommend removing from the policies and procedures. Resolution: This reference has been removed from the draft of the policies and procedures manual. The final policies and procedures manual will be issued after appropriate supervisors have reviewed and issued their approval.*

**COMMONWEALTH OF KENTUCKY  
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**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC6-28: The Cabinet For Families And Children Should Require State Colleges, Universities, And Area Development Districts To Submit An Annual Audit Report (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Issue: APA noted the continuing problem with the turnaround time of audits sent to OIG for A-133 desk reviews. Resolution: CMB has requested OIG to follow-up and complete the audits previously sent. We understand that OIG is short on staff and may not be able to complete the desk reviews in a timely manner without additional staff.*

*Issue: Audits for 2002 were not submitted or desk reviews not performed as follows - the Childcare Council of Kentucky audit for 2002 was not submitted. Resolution: This vendor had not submitted an audit in the past three years. The CMB auditor sent non-compliance letters to the vendor and had telephone conversations with the executive director and has since received and reviewed audits for 1999 – 2000. In our telephone conversation Monday, March 1, 2004, with the agency's executive director, he assured us that Childcare Council of KY would have their 2001-2002 A-133 audit to us by March 15, 2004. Future audits would be performed in a timely manner and submitted to CMB. CMB or OIG will perform the desk review of the audit once received.*

*Jefferson County Attorney: No desk review was performed for the 2002 audit. Resolution: This audit was sent to OIG on April 1, 2003. At a meeting with OIG, we requested the audit be given priority and have since requested from OIG a status report of these audits. We understand that OIG is short on staff and may not be able to complete the desk reviews in a timely manner without additional staff.*

*Kenton County Attorney: No desk review was performed for the 2002 audit. Resolution: This audit was sent to OIG on September 23, 2003. At a meeting with OIG, we requested the audit be given priority and have since requested from OIG a status report of these audits. We understand that OIG is short on staff and may not be able to complete the desk reviews in a timely manner without additional staff.*

*Pike County Attorney: The audit for 2002 not submitted. Resolution: A non-compliance letter was sent to the county attorney on 2/23/04. Several telephone calls were made prior to sending the letter. The Pike County Attorney's office assumed that they were under the \$300,000 limit for an A-133 audit. They had*

**COMMONWEALTH OF KENTUCKY  
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**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC6-28: The Cabinet For Families And Children Should Require State Colleges, Universities, And Area Development Districts To Submit An Annual Audit Report (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*auditors performing their 2003 audit at the time of our telephone calls. CMB staff requested an engagement letter for the 2002 and the approximate date the 2002 audit could be completed. Due to the limitations of the Management Administrative Reporting System and Seagate reporting of two-year contracts, CMB did not have this facility in the schedule for an A-133 audit. CMB will follow through on obtaining a 2002 audit and performing a desk review. We will set up an additional monitoring process for reviewing two-year contract requirements of an A-133 audit. Note that CMB is limited with only one audit staff member and will need additional auditors if OIG cannot perform these.*

*Bluegrass ADD: No desk review was performed for the 2002 audit. Resolution: The CMB will require submission of ADD audits and complete desk reviews. Note that CMB is limited with only one audit staff member and will need additional auditors if OIG cannot perform these.*

*City of Louisville: No desk review was performed for the 2002 audit. CMB's contract is with the Louisville/Jefferson County CAA. Resolution: OIG sent CMB an engagement letter dated June 23, 2003 for City of Louisville, Louisville-Jefferson Community Action Agency, and Low-Income Home Energy Assistance Program. This audit was performed by OIG and CMB is working with OIG to resolve the completion of the audit report. At a meeting with OIG, we requested the audit be given priority. We understand that OIG is short on staff and may not be able to complete the desk reviews in a timely manner without additional staff.*

*U.K. Research Foundation: The audit for 2002 was not submitted. Resolution: CMB will obtain a copy of the U.K. Research Foundation 2002 audit and perform a desk review. Note that CMB is limited with only one audit staff member and will need additional auditors if OIG cannot perform these.*

*Kentucky Community & Technical College System: An audit for 2002 was not submitted. Resolution: CMB will obtain a copy of the Kentucky Community & Technical College System's 2002 audit and perform a desk review. Note that CMB is limited with only one audit staff member and will need additional auditors if OIG cannot perform these.*



**COMMONWEALTH OF KENTUCKY  
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**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC6-28: The Cabinet For Families And Children Should Require State Colleges, Universities, And Area Development Districts To Submit An Annual Audit Report (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Big Sandy ADD: No desk review was performed for the 2002 audit. Resolution: CMB will perform a desk review on the Big Sandy ADD 2002 audit. Note that CMB is limited with only one audit staff member and will need additional auditors if OIG cannot perform these.*

*Because multiple agencies in CHFS have contracts with the same vendors/agencies, we recommend the consolidation of the desk review auditing process. This change would eliminate duplication of effort and would provide more effective oversight of contracts. The OIG could perform one (1) desk review on a vendor's audit, and then furnish the determination letter of findings to all appropriate agencies within the Cabinet.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC7-29: The Cabinet For Families And Children Should Discontinue Temporary Assistance For Needy Families Benefits To Recipients Who Have Reached The Sixty Month Lifetime Limit**

State Organization: Cabinet for Families and Children

Federal Program: CFDA 93.558 - Temporary Assistance for Needy Families

Federal Agency: U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Eligibility, Activities Allowed/Unallowed, and Allowable Costs

Amount of Questioned Costs: \$8,876

The Federal Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Public Law 104-193, as amended) mandated a maximum lifetime limit on welfare benefits for 60 months. Some households scheduled to have their benefits discontinued may receive special hardship exemptions and may continue to receive all or a portion of their TANF cash assistance for as long as the hardship lasts.

We tested a sample of 25 TANF recipients that had reached 60-month lifetime limit to determine if benefits received beyond the 60 months were supported by a valid extension. We found five (5) instances where clients received over 60 months of benefits and evidence to support a valid extension could not be produced. We also found a sixth instance of this in another test we performed.

<b>Case Number</b>	<b>Number of ineligible months</b>	<b>Monthly benefit amount</b>	<b>Ineligible amount client received</b>
1	14	\$ 225	\$ 3,150
2	16	128	2,048
3	2	328	656
4	5	225	1,125
5	4	328	1,312
6	2	Various	585
		<b>Total</b>	<b>\$ 8,876</b>

When CFC fails to discontinue benefits to TANF recipients that have reached the 60-month lifetime limit, clients receive additional money that they are not entitled to, which may prevent eligible recipients from receiving benefits due to the limited funds available. In addition, failing to discontinue benefits at 60 months (without evidence to support a valid extension) could result in the state being penalized by the Department of Health and Human Services.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC7-29: The Cabinet For Families And Children Should Discontinue Temporary Assistance For Needy Families Benefits To Recipients Who Have Reached The Sixty Month Lifetime Limit (Continued)**

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The OMB Circular A-133 Compliance Supplement for CFDA 93.558 Part III. E.1.b. (1) states, “Any family that includes an adult or minor child head of household or a spouse of the head of household who has received assistance under any State program funded by Federal TANF funds for 60 months (whether or not consecutive) is ineligible for additional federally funded TANF assistance.”

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 Section 408 (a) (7) (A) states

NO ASSISTANCE FOR MORE THAN 5 YEARS – IN GENERAL – A State to which a grant is made under section 403 shall not use any part of the grant to provide assistance to a family that includes an adult who has received assistance under any State program funded under this part attributable to funds provided by the Federal Government, for 60 months (whether or not consecutive) after the date the State program funded under this part commences . . .

TANF Final Rule Executive Summary states, “In general, States may not use Federal Funds to provide assistance to a family if it includes an adult or minor head-of-household or the spouse of a head-of-household who has received assistance for a cumulative total of more than 60 months.”

Federal Regulations at 45 CFR 264.1(a)(1), state, “Subject to the exceptions in this section, no State may use any of its Federal TANF funds to provide assistance to a family...who has received Federal assistance for a total of five years (i.e., 60 cumulative months, whether or not consecutive).”

Federal Regulations at 45 CFR 264.2, also states:

If we determine that a State has not complied with the requirements of §264.1, we will reduce the SFAG payable to the State for the immediately succeeding fiscal year by five percent of the adjusted SFAG unless the State demonstrates to our satisfaction that it had reasonable cause, or it corrects or discontinues the violation under an approved corrective compliance plan.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC7-29: The Cabinet For Families And Children Should Discontinue Temporary Assistance For Needy Families Benefits To Recipients Who Have Reached The Sixty Month Lifetime Limit (Continued)**

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**Recommendation**

Although evidence to support a valid extension could not be produced in three (3) of the five (5) counties we visited, we did note that valid extensions were well documented in several cases. However, since this was a finding in the FY 02 audit and since multiple problems were found again in FY 03, we recommend the following:

- CFC should remind staff statewide of the importance of closely monitoring each case so that an ineligible recipient does not receive additional months of benefits to which they are not entitled.
- Caseworkers should request and retain adequate documentation in the recipient files to support extensions of benefits beyond the lifetime limit.
- Extensions should be reviewed timely in accordance with CFC's policies and procedures.
- Funds issued in error should be recouped from the client, if at all possible.
- CFC should reimburse the federal government for the noted questioned costs.
- A control should be programmed into the Kentucky Automated Management and Eligibility System (KAMES) so the Kentucky Transitional Assistance Program (K-TAP) cases approaching the 60-month lifetime limit will not be recertified without a valid extension code and a supervisor's approval.

**Management's Response and Corrective Action Plan**

*From the Family Support perspective, field staff are supposed to be checking the cases on their 36-month listing (this contains K-TAP cases containing an adult that has received 36 months or more of TANF benefits) monthly on RMDS. This report also contains cases receiving 60 months or more. Cases facing discontinuance due to the 60-month time limit must be manually reviewed two (2) months prior to their potential date of discontinuance. At this point, the worker should be checking the tracking screens on months of TANF receipt to ensure the file is correct and make any corrections (deletions or additions) if necessary. The case should also be reviewed at this time to see if the household meets any of the 20% hardship criteria to receive beyond 60 months.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
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(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC7-29: The Cabinet For Families And Children Should Discontinue Temporary Assistance For Needy Families Benefits To Recipients Who Have Reached The Sixty Month Lifetime Limit (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Division of Family Support (DFS) is going to send out a memo reminding field staff of these procedures and require supervisory review of the listing monthly to ensure those nearing the 60-month time limit are taken care of appropriately. We will also do a monthly email to supervisors when the listing is produced and cc regional office program specialist, coordinators and service region administrators and service region administrator assistants.*

*The 60-month extension reports on RDS are supposed to be utilized by field staff monthly to ensure the cases are in qualified extensions and are reviewed at the proper interval and determined ongoing eligible for the extension. This listing should be used to ensure cases are discontinued if the household is no longer eligible for an extension. Cases on the 60-month extension list coded "N" (not eligible for the 60-month extension) should be reviewed monthly to determine why the case has received beyond 60 months without being coded to an eligible extension reason. There are some problems with the report and some cases are on the list that have not received 60 months (e.g., fugitive felons who are technically excluded from the K-TAP grant and the listing also picks up months the K-TAP adult may have received K-TAP as a teen parent).*

*DFS is going to send a monthly reminder with the 60-month extension reports are posted to RDS and require listings to be annotated and reviewed at the regional level monthly. DFS will review the annotated 60-month listings on a quarterly basis.*

*The KAMES system contains a count to track the 60 months of allowed receipt of federal TANF funds. However, that count can be adjusted to include months of receipt of TANF benefits from other states that operate under a waiver of non-countable months due to the age of the specified relative. Per 45 CFR 264.1(c) states are allowed to extend assistance paid for by the federal TANF funds beyond the five year limit for up to 20 percent average monthly number of families receiving assistance during the fiscal year or the immediately preceding fiscal year, which ever the state elects. Currently, Kentucky extends less than 1% of its average caseload.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC7-29: The Cabinet For Families And Children Should Discontinue Temporary Assistance For Needy Families Benefits To Recipients Who Have Reached The Sixty Month Lifetime Limit (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Per 45 CFR 264.2, if it has been determined a state has failed to comply with the federal five (5) year time limit; the state will incur a 5% reduction in its State Family Assistance Grant (SFAG) in the next fiscal year. However, if the state can demonstrate reasonable cause or corrects or discontinues the violation under an approved corrective compliance plan the penalty would be waived.*

*Per 45 CFR 260, et al., if a state is found to not be in compliance with program requirements, the penalty is assessed through a reduction in the SFAG. With the exception of failing to repay a federal loan, remitting contingency funds if criteria is not met or replacing penalty reduction with state funds. States are not required to repay federal TANF funds.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC8-30: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services**

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State Organization: Cabinet for Families and Children

Federal Program: CFDA 93.558 - Temporary Assistance for Needy Families

Federal Agency: U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Eligibility, Activities Allowed/Unallowed and Allowable Costs

Amount of Questioned Costs: \$5,791

We tested a sample of 77 payments to participants in the TANF program. CFC failed to produce records to support expenditures and follow procedures outlined in *Volume III - Kentucky Transitional Assistance Program* of its operating manual.

We noted the following weaknesses:

- Recipient files were missing for four (4) cases selected, resulting in questioned costs of \$1,702.
- Recipient applications or recertifications from FY 03 were missing in three (3) cases tested, resulting in questioned costs of \$2,723.
- Receipts for two (2) supportive service payments could not be produced, resulting in questioned costs of \$968.
- Incomplete PA-32 was noted in one (1) case (unused lines were not crossed out on the form).
- Out-of-state birth certificates were not produced for two (2) cases.
- Birthdate (month and year) of children in three (3) cases were entered incorrectly into KAMES.
- Signed K-TAP applications could not be produced for two (2) cases, resulting in questioned costs of \$398.
- Other application documents were not found in various cases when required.

CFC has not taken adequate measures to correct these problems, as similar problems were noted in the FY 01 and FY 02 audits. We did note, however, that there has been significant improvement regarding maintaining PA-32s for expenditures, and CFC should be commended for their efforts towards the correction of this problem.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC8-30: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services (Continued)**

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There are numerous effects of the above weaknesses, including:

- If entire case files, K-TAP applications/recertifications, and receipts for expenditures, cannot be located, CFC and the Department for Health and Human Services (DHHS) cannot be assured benefits are issued to eligible recipients.
- If PA-32s are not completed according to instructions, the potential for fraud and misuse of funds exists.
- If out-of-state birth certificates are not requested for client dependents, authoritative support for the dependency relationship cannot be assured.
- If dependent birth dates are not entered correctly into the system, benefits might be paid for an otherwise ineligible recipient.
- Without obtaining signed forms from clients during the application/recertification process, the applications/recertifications will not be complete. In addition, all of the information required to be communicated may not be and evidence of this communication could not be verified by CFC and the client.

Federal Regulations at 45 CFR 92.20 (a)(2), state, “fiscal control and accounting procedures of the State...must be sufficient to...permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.”

Federal Regulations at 45 CFR 92.42(b)(1), also state, “. . . records must be retained for three years from the starting date specified in paragraph C.”

Good internal controls dictate that procedures be followed to ensure payments are made only for approved and allowable goods and services.

**Recommendation**

Since these problems were found in various counties throughout the state, we recommend CFC remind caseworkers statewide that:

- Case files should be produced and maintained to adequately support expenditures.
- An adequate filing system should be maintained so that case files may be located.



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC8-30: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services (Continued)**

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**Recommendation (Continued)**

- Lines not used on the form PA-32 should be crossed out.
- Receipts for all supportive service payments should be requested and maintained.
- Birth certificates for out-of-state dependents should be requested and maintained.
- CFC should remind staff of the importance of maintaining an accurate and complete participant case file.
- Funds should be returned to the federal government as a result of the questioned costs.

**Management's Response and Corrective Action Plan**

*County A: Monitoring of families who have received over 52 months is in place in County A at this time with our Pro Team meetings. We will continue this process and comment on any possible extension of TANF funds past 60 months. A red color label will be added to Kentucky Works Program (KWP) case files when a participant reaches 36 months. Now that all case records are kept in one office (no longer on contract with Community Action Council), no loss of case records is expected in the future so documentation and verification will not be an ongoing problem. We will go over in regular staff meeting the importance of monitoring 60 month plus cases and pay close attention to extension dates according to policy and procedure. We will also go over in staff meeting the completion of PA32's and crossing out unused lines. All PA32's in excess of \$99 are co-signed by a supervisor or KWP coordinator. Again, with all cases now controlled by the region, we should not have errors on PA32's and they will be in the case record with a receipt attached. If ever a case does exceed 60 months with no extension code in place, a claim will be processed to recoup benefits issued in error. County A has new guidelines for case readings in place immediately. We will be reading 40 plus KTAP/KWP cases per month on case actions, applications and recertifications on 13 case managers who are fully trained and reading completely on one case manager who does not yet have case decision. This will help in having all proper documents signed and required forms in the case record. All inactive KWP folders are now kept in a separate filing area and will be available for review.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC8-30: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*County B: In response to the deficiency noted for County B of a 101 with no signature, the corrective action is as follows: Personnel with Family Support will review with all staff at staff meeting the importance of having all appropriate forms in the case record with the appropriate signatures and personnel will monitor all case readings for the month of March 2004 for proper forms and signatures with a goal of 100% compliance.*

*County C: There were three issues identified in the TANF audit for County C: lack of out-of-state birth certificates in two cases, lack of a signed CS-333 in two (2) cases and an incorrect DOB entered on KAMES. Each of these exceptions has been or will be addressed with staff.*

*The out-of-state birth certificate issue was addressed with all case management staff at our monthly case managers' meeting on 3/1/04. The policy regarding verification requirements of out-of-state births as well as the correct procedures to follow-up and ensure that the birth verification is received and placed in the case record in a timely manner were reviewed. This policy will also be reviewed at a monthly supervisors' meeting on March 11, 2004. County C family support supervisors attend this meeting.*

*The supervisors' meeting on March 11, 2004 will also provide us with a forum to address the CS-333 issue. The specific problem we had seemed to involve having the client sign the form when he/she is reapplying for KTAP. Our program specialist will review the procedural instructions for this form to ensure that we are having the CS-333 signed at appropriate times.*

*The final exception cited involved an incorrect date of birth (DOB). The worker had entered 12/8/89 instead of 10/8/89 for a child on the case. It was clearly a data entry error and did not affect potential eligibility for benefits in any way. The DOB has been corrected and we will remind workers to be careful when making all system entries.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC8-30: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*County C (Continued): Also cited in the audit was the fact that we were not able to locate 2 of the 38 cases requested by the auditor. Both of these cases were listed under test number 4, for which five (5) additional cases were requested as "Alternates if any of the above items from Test 4 cannot be located." Because we were able to locate all 5 alternates, we may have misjudged the gravity of not locating two (2) cases in the original group.*

*A primary cause for us not being able to find one (1) of the cases was that we were in the midst of a crisis in our discontinued files. Due to flooding in the basement earlier in the year and a pending project to relocate the discontinued files while the flooding was addressed, we had over 300 boxes of unfiled discontinued cases. We did find several discontinued cases for tests 1-3 in the audit by going through these boxes manually. However, because alternates were listed for the two (2) cases now cited in the audit, we may not have searched as diligently for them.*

*The issue of the discontinued files continues to be addressed. The unfiled cases are now boxed in alphabetical order and will be moved back into the file cabinets as soon as the work in the basement is completed.*

*The amounts listed as projected costs for the two (2) cases that we could not locate are much higher than the benefits these clients actually received in FY 2003. For case number 63, the loss for FY 2003 is projected to be \$7200 (12 months of Kinship care at \$600 per month).*

*However, the amount actually received in the FY 2003 for this case was \$3300 (\$300 received in 9/02 and \$600 received in each month between 10/02 and 02/03). For case number 77, the projected loss was \$9000 (12 months at \$750 per month). However, the \$750 in question was an Employment Retention Assistance (ERA) payment that was issued in 6/02. ERA was not an ongoing, monthly payment. Rather it was a set amount of money (\$1500) that was available to former K-TAP recipients whose cases discontinued with wages and who needed financial assistance to remain employed. Because the maximum ERA payment was \$1500, the loss could not have exceeded that amount. In fact, the client in question exhausted her ERA funds in 6/02, so there would not have been any funds left to use in FY 2003.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC8-30: The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*Through our monthly case managers' meeting and our monthly supervisors' meeting, we address policy issues and concerns on a regular basis. We will continue to use these meetings as part of our ongoing efforts to provide quality casework and quality customer service to the families we assist.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC10-31: The Cabinet For Families And Children Should Disburse Child Support Grant Funds In Compliance With Federal Requirements**

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State Organization: Cabinet for Families and Children  
Federal Program: CFDA 93.563 – Child Support Enforcement  
Federal Agency: U.S. Department of Health and Human Services  
Pass-Through Agency: Not Applicable  
Compliance Area: Activities Allowed/Unallowed  
Amount of Questioned Costs: None

We tested FY 03 CSE grant expenditures and found CFC advanced funds to contractors that perform child support case services. Specifically, seven (7) out of 59 expenditures examined were payments made to contractors that had not yet incurred costs, nor submitted documentation of actual expenses for reimbursement. The state processes the advances in the federal fund and is reimbursed by the federal government. CFC then recoups advanced funds over the course of the fiscal year by reducing subsequent billings received from contractors.

CFC is not disbursing CSE grant funds in compliance with federal requirements.

The OMB Circular A-133, Compliance Supplement Part 3, Section B, Allowable Costs/Cost Principles, Compliance Audit Procedures for State, Local, and Indian Tribal Governments, states in part that allowable costs “represent charges for actual costs, not budgeted or projected amounts.”

We contacted DHHS, Administration for Children and Families, Frequently Asked Questions support staff and they stated “it is fine for the state to advance the funds to the contractor, but they cannot claim federal reimbursement until they have an invoice for the actual expenditure for the services. The federal regulations and OMB Circular would override the state's contractual procedures.”

**Recommendation**

We recommend that CFC either no longer advance CSE grant funds to contractors from the state's federal fund or obtain a waiver from the federal government permitting the state to advance funds to contractors.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING: 03-CFC10-31: The Cabinet For Families And Children Should Disburse  
Child Support Grant Funds In Compliance With Federal Requirements  
(Continued)**

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**Management's Response and Corrective Action Plan**

*We did not realize that state funds were not being used for the installment payments to child support contracting officials. In the future we will either stop the practice of installment payments or issue payments utilizing state funds only.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-FAC8-10: The Finance And Administration Cabinet Should Track  
Federal Expenditures For The Jobs And Growth Tax Relief Reconciliation Act In  
The Management Administrative And Reporting System**

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State Organization: Finance and Administration Cabinet

Federal Program: CFDA 21.999 - Jobs And Growth Tax Relief Reconciliation Act

Federal Agency: U.S. Department of Treasury

Pass-Through Entity: Not Applicable

Compliance Area: Activities Allowed/Unallowed and Allowable Costs/Cost Principles

Amount of Questioned Costs: None

This finding is a reportable condition for internal controls over financial reporting and for internal control over compliance. The entire finding can be found in the financial statement findings as 03-FAC8-10. Finding 03-FAC8-10 explains the circumstances that resulted in a scope limitation and the qualification on the auditor's report on compliance.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST1-32: The Justice Cabinet Should Either Develop An Indirect Cost Allocation Plan And Submit It To The Cognizant Federal Agency For Approval Or Stop Charging Indirect Costs To The Federal Government**

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State Organization: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575-Crime Victim Assistance

CFDA 16.579-Byrne Formula Grant Program

CFDA 16.588-Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs/Cost Principles

Amount of Questioned Costs: \$46,774

Indirect costs are those costs that benefit common activities and, therefore, cannot be readily assigned to a specific direct cost objective or project. As we noted during the FY 02 audit, although the Justice Cabinet, Office of the Secretary, Grants Management Branch (GMB) does not have an approved indirect cost plan in place for charging indirect costs to federal grants, indirect costs are included as part of the administrative costs for the agency. In Management's Response to the FY 02 audit finding concerning indirect costs, the GMB stated:

*As recommended, the Justice Cabinet, Office of the Secretary will obtain the necessary information to formulate an indirect cost plan. Once formulated, the plan will be submitted to our federal cognizant agency for approval. The GMB will provide assistance to the Division of Administration as needed. The Justice Cabinet, Office of the Secretary will notify the APA if any problems are encountered.*

As of the date of this comment for the FY 03 audit, no action has been taken to correct this deficiency.

Charging indirect costs to federal grants without an approved indirect cost plan in place is not in compliance with OMB Circular A-133, Compliance Supplement Part 3 - Compliance Requirements, Section B. Allowable Costs/Cost Principles, which states, "In order to recover indirect costs, organizations must prepare cost allocation plans (CAPs) which apply only to state, local and Indian tribal governments or indirect cost rate proposals (IDCRPs) in accordance with the guidelines provided in OMB's Circulars."



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST1-32: The Justice Cabinet Should Either Develop An Indirect Cost Allocation Plan And Submit It To The Cognizant Federal Agency For Approval Or Stop Charging Indirect Costs To The Federal Government (Continued)**

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According to the U.S. Department of Justice Financial Guide, Chapter 17, Indirect Costs,

In order to be reimbursed for indirect costs, a recipient must first establish an appropriate indirect cost rate. To do this, the recipient must prepare an indirect cost rate proposal and submit it to the cognizant Federal agency . . . If an indirect cost proposal for recovery of actual indirect costs is not submitted to the cognizant Federal agency within three months of the start of the award period, indirect costs will be irrevocably lost for all months prior to the month that the indirect cost proposal is received. This policy is effective for all awards.

**Recommendation**

We recommend the GMB develop an appropriate indirect cost plan and submit it to the federal cognizant agency for approval.

Since the GMB does not currently have an approved indirect cost plan in place, we recommend that no further indirect costs be charged to these grants and that any indirect costs charged to the grants for FY 04 be reversed.

We are questioning approximately \$46,774 in costs charged to the three (3) grants included in this audit as improperly charged indirect costs for FY 03.

**Management's Response and Corrective Action Plan**

*The Justice and Public Safety Cabinet concurs with the need for an indirect cost plan and is now in the process of developing a draft for U.S. Department of Justice review. The Cabinet anticipates forwarding the draft by March 31, 2004. The Cabinet will seek direction from the U.S. Department of Justice, Office of the Comptroller, regarding FY 2003 and 2004 indirect costs incurred prior to the completion of the plan.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST2-33: The Justice Cabinet Should Follow Established Subrecipient Monitoring Policies And Procedures To Ensure Subrecipient Monitoring Is Properly Performed And Documented**

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State Organization: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575-Crime Victim Assistance

CFDA 16.579-Byrne Formula Grant Program

CFDA 16.588-Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: None

In the Crime Victim Assistance (VOCA) and Violence Against Women (VAWA) subrecipient files that we reviewed for the FY 03 audit, there were several instances of files without either financial or programmatic monitoring tools completed during the fiscal year. In addition, we noted quarterly subgrantee progress, financial reports, and closeout reports not submitted timely to GMB by subrecipients.

In the Byrne subrecipient files that we reviewed for FY 03, there were some financial reports received several months past the due date, causing payments to be delayed for these entities. We also noted very few site visits documented. Two (2) of the subrecipients had not yet submitted final reports for the grant.

Without adequate documentation in the subrecipient files, it is not possible to determine what monitoring activities are performed or how often they are performed.

During FY 03, sufficient monitoring activities were not being performed and/or documented to ensure subrecipients were using federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals were achieved. Subrecipients could be in noncompliance with federal requirements and grant funds could be spent erroneously when monitoring is not performed adequately or timely.

According to OMB Circular A-133, Subpart D (d) Pass-through entity responsibilities,

A pass-through entity shall perform the following for the federal awards it makes: . . .

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST2-33: The Justice Cabinet Should Follow Established Subrecipient Monitoring Policies And Procedures To Ensure Subrecipient Monitoring Is Properly Performed And Documented (Continued)**

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- (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

Policies and procedures for subrecipient monitoring should be in place and followed to ensure subrecipients are spending federal grant funds in compliance with their grant agreement as well as federal laws and regulations.

**Recommendation**

During FY 03, GMB developed a specific set of procedures to monitor subrecipient activity. The procedures are outlined in the GMB policies and procedures manual.

A monitoring schedule has been implemented to determine which subrecipients will receive desk, telephone, or site monitoring reviews. Various risk factors are used to determine the need for site visits to subrecipients. The site monitoring schedule showed a listing of all subrecipients and the dates for the financial and programmatic visits. By viewing this schedule, it is easy to see where GMB has made site visits and where there is still a need.

We reviewed several subrecipient files that had site visits documented during FY 04. We noted that in these files there was sufficient documentation of both financial and programmatic site visits. These files contained updated applications and evidence of a review of supporting financial data submitted by subrecipients.

We recommend the GMB continue to implement policies and procedures to ensure subrecipient monitoring activities are being performed consistently and on a regular basis. We further recommend that documentation of these activities be filed in the subrecipient files when performed. We believe the addition of personnel to the GMB has greatly improved the monitoring of subrecipients and will help the GMB comply with federal monitoring requirements in the future. We recommend that this commitment of additional personnel to the improvement of grant compliance activities be continued so that all federal grant compliance requirements can be met.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST2-33: The Justice Cabinet Should Follow Established Subrecipient Monitoring Policies And Procedures To Ensure Subrecipient Monitoring Is Properly Performed And Documented (Continued)**

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**Management's Response and Corrective Action Plan**

*The Justice and Public Safety Cabinet concurs with the finding and recommendation, and will continue to implement the corrections already instituted and noted above.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST3-34: The Justice Cabinet Should Continue To Develop Procedures To Ensure Subrecipients That Expend More Than \$300,000 In Federal Awards In A 12 Month Period Receive An OMB Circular A-133 Audit**

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State Organization: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575-Crime Victim Assistance

CFDA 16.579-Byrne Formula Grant Program

CFDA 16.588-Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: None

For the subrecipient files reviewed during the FY 03 audit, we noted that the GMB did not perform sufficient subrecipient monitoring activities to ensure subrecipients expending more than \$300,000 in Federal awards receive OMB Circular A-133 audits.

We also noted for those subrecipients that had audits on file at the GMB, there were some that did not have documentation of a desk review performed on the audit or record of follow up on audit findings.

During FY 03, the GMB was not in compliance with OMB Circular A-133, Compliance Supplement Part 3 - Compliance Requirements, Section M. Subrecipient Monitoring, by not requiring all subrecipients that expend more than \$300,000 in federal awards to provide current audits to the GMB and not performing desk reviews of audits or following up on audit findings.

According to the Code of Federal Regulations, Chapter 2 (28 CFR 66.26), (a) “Grantees and subgrantees are responsible for obtaining audits in accordance with the Single Audit Act Amendments of 1996 and revised OMB Circular A-133.”

According to OMB Circular A-133, Subpart D (d) Pass-through entity responsibilities.

A pass-through entity shall perform the following for the federal awards it makes: . . .

- (2) Advise subrecipients of requirements imposed on them by Federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirement imposed by the pass-through entity.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST3-34: The Justice Cabinet Should Continue To Develop Procedures To Ensure Subrecipients That Expend More Than \$300,000 In Federal Awards In A 12 Month Period Receive An OMB Circular A-133 Audit (Continued)**

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- (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- (4) Ensure that subrecipients expending \$300,000 or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
- (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.
- (6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.

**Recommendation**

During FY 04, GMB has implemented an audit-tracking schedule designed to determine which subrecipients are required to have an OMB Circular A-133 audit and document whether the audit has been received.

We recommend GMB continue to develop procedures to ensure subrecipients that expend more than \$300,000 in Federal awards in a 12 month period receive an OMB Circular A-133 audit. We further recommend that GMB review the audits and follow up on audit findings within six (6) months after receipt of the audit. The audit desk review and follow up of audit findings should be properly documented in the subrecipient's file.

**Management's Response and Corrective Action Plan**

*The Justice and Public Safety Cabinet concurs with the finding and recommendation, and will continue to implement the corrections already instituted and noted above.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST4-35: The Justice Cabinet Should Ensure Information On The Quarterly Financial Status Reports Is Reliable**

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State Organization: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575-Crime Victim Assistance

CFDA 16.579-Byrne Formula Grant Program

CFDA 16.588-Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Costs: None

We reviewed the June 30, 2003 quarterly SF 269A Financial Status Reports submitted by the GMB to determine if they were supported by sufficient, accurate documentation.

We noted that amounts on the reports we reviewed were not adequately supported by MARS documentation. The supporting documentation used by the agency was the internal spreadsheet that tracks expenditures of the subrecipients' federal share and local match, known as the "cashbook." The cashbook was not reconciled to MARS.

Since the SF 269A reports contain the actual expenditures and unliquidated obligations as incurred for both the reporting period and, cumulative for the award period, it is important that the amounts on the report be supported in the agency's accounting records.

Since the reports are providing cumulative information, incorrect accounting information could affect numerous reporting periods.

According to the U.S. Department of Justice Financial Guide, Chapter 11: Reporting Requirements, "Grantees are also required to maintain adequate documentation to provide an audit trail that substantiates the amounts reported on each SF 269A as submitted."

**Recommendation**

GMB personnel informed us that they were no longer using the cashbook for FY 04. Instead, they post local match and program income data to a report when a financial report is entered into MARS. Since the local match and program income information from the financial reports is not currently entered into MARS, this report, called the status report provides supplemental information for the SF 269A. The federal expenditure portion of the status report is reconciled monthly

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST4-35: The Justice Cabinet Should Ensure Information On The  
Quarterly Financial Status Reports Is Reliable (Continued)**

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**Recommendation (Continued)**

to MARS. We reviewed SF 269A reports for the December 31, 2003 quarter and found the information on the report traces to the supporting documentation. We feel the SF 269A reports prepared using the MARS report and the status report are accurate and meet federal reporting requirements.

We recommend the GMB continue to use the improved reports and continue the monthly reconciliation with MARS. We recommend the GMB try to improve the internally generated status report to accurately reflect the quarter's expenditures as well as cumulative expenditures for the local governments federal share and local match.

**Management's Response and Corrective Action Plan**

*The Justice and Public Safety Cabinet concurs with the finding and recommendation, and will continue to implement the corrections already instituted and noted above.*



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST5-36: The Justice Cabinet Should Implement Its Corrective Action Plan For Weaknesses Noted In Prior Year Regarding Indirect Costs**

State Organization: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575-Crime Victim Assistance

CFDA 16.579-Byrne Formula Grant Program

CFDA 16.588-Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs/Cost Principles

Amount of Questioned Costs: None

Justice Cabinet, Office of the Secretary, GMB has not implemented its corrective action plan for indirect costs, therefore materially misrepresenting the FY 2002 corrective action plan. The GMB did not develop and implement an Indirect Cost Allocation Plan for charging indirect costs to various federal grants.

Failing to implement the corrective action plan stated in the FY 02 audit finding results in the agency still not complying with OMB Circular A-133, Compliance Supplement Part 3 - Compliance Requirements, Section B. Allowable Costs/Cost Principles. Therefore, the GMB is continuing to charge indirect costs to federal grants without an approved indirect cost plan in place.

OMB Circular A-133 Part A, Subpart E\_\_\_.500 states:

Audit follow-up. The auditor shall follow-up on prior audit findings, perform procedures to assess the reasonableness of the summary schedule of prior audit findings prepared by the auditee in accordance with §\_\_\_.315(b), and report, as a current year audit finding, when the auditor concludes that the summary schedule of prior audit findings materially misrepresents the status of any prior audit finding. The auditor shall perform audit follow-up procedures regardless of whether a prior audit finding relates to a major program in the current year.

**Recommendation**

We recommend GMB implement its corrective action plan previously submitted to auditors. GMB should ensure an Indirect Cost Allocation Plan be established and submitted to the federal cognizant agency for approval. The GMB should then apply the plan when charging all indirect costs to federal grants.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-JUST5-36: The Justice Cabinet Should Implement Its Corrective Action Plan For Weaknesses Noted In Prior Year Regarding Indirect Costs (Continued)**

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**Management’s Response and Corrective Action Plan**

*Although the Justice and Public Safety Cabinet agrees with the need for an indirect cost plan, it disagrees with the implication that there was a “material misrepresentation” made to the Office of the Auditor of Public Accounts or its staff. The FY 2002 audit finding directing the Cabinet to complete an Indirect Cost Allocation Plan was received in draft form in February 2003. Shortly after that date, the task was assigned to the Cabinet’s Division of Administration, and research into the process was begun. This was communicated to the Office of the Auditor of Public Accounts by memo from the Secretary of the Justice Cabinet, March 3, 2003. Progress on this task was interrupted by the retirement of the manager of the Grants Management Branch in July 2003 and a delay in replacing the Cabinet’s Budget Director, who had resigned in January 2003. These positions were not re-filled until October 2003 and July 2003, respectively. When the new Grants Management Branch manager was hired, she assumed responsibility for this task and has been in communication with the U.S. Department of Justice regarding development and submission. A draft plan is now scheduled for submission to the U.S. Department of Justice by March 31, 2004.*

**Auditor’s Reply**

While we acknowledge that the GMB has recently started developing an indirect cost plan, there was no evidence found during the audit that any work on an indirect cost plan had been done during FY 03. We feel that the “material misrepresentation of prior year audit finding” accurately reflects the status of this audit finding.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-MIL2-37: The Department Of Military Affairs Should Implement A System To Properly Monitor Subrecipient Activities To Comply With OMB Circular A-133 Compliance Requirements**

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State Organization: Department of Military Affairs  
Federal Program: CFDA 83.544 – Public Assistance Grants  
Federal Agency: U.S. Federal Emergency Management Agency  
Pass-Through Agency: Not Applicable  
Compliance Area: Subrecipient Monitoring  
Amount of Questioned Costs: None

As part of our compliance testing, we tested the Department of Military Affairs' (DMA) system for monitoring and tracking subrecipient activity. The results of our testing indicated there were deficiencies in monitoring subrecipients receiving funds in excess of \$300,000. We noted that not all entities receiving funds in excess of \$300,000 had filed audit reports; one (1) entity still has not submitted an audit report. We also noted that two (2) entities had filed audit reports late (past the 9-month reporting period required by OMB Circular A-133).

In previous audits of the DMA, we noted a lack of an adequate system for monitoring its subrecipients; we acknowledge that attempts at monitoring and tracking are being made and that improvements have been made. There is evidence that DMA provides adequate notification of OMB Circular A-133 requirements initially, at in-take for disaster projects and during the forwarding of funding. However, there does not appear to be a complete follow through with those entities receiving in excess of \$300,000.

The DMA cannot be assured that the subrecipients (applicants) are complying with the requirements of OMB Circular A-133 without having an adequate monitoring system in place and ensuring that those entities receiving \$300,000 or more in federal funds provide audits in a timely fashion.

OMB Circular A-133, Subpart B states: “[N]on-Federal entities that expend \$300,000 or more in a year in Federal awards shall have a single or program-specific audit conducted for that year in accordance with the provisions of this part.”

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-MIL2-37: The Department Of Military Affairs Should Implement A System To Properly Monitor Subrecipient Activities To Comply With OMB Circular A-133 Compliance Requirements (Continued)**

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In addition, according to OMB Circular A-133, Subpart D - Federal Agencies and Pass-through Entities, Section .400, a pass-through entity shall perform the following for the Federal awards it makes:

- Advise subrecipients of requirements imposed on them by Federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.
- Monitor the activities of subrecipients as necessary to ensure Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are met.
- Ensure that subrecipients expending \$300,000 or more in Federal awards during the Subrecipient's fiscal year have met audit requirements.
- Issue a management decision on those audit findings which impact the compliance with OMB A-133 within six (6) months after receipt of the subrecipient's audit report. Additionally, ensure that the subrecipient takes appropriate and timely corrective action.
- During monitoring and tracking consider whether the subrecipient audits necessitate adjustment of the pass-through entity's own records after review of the subrecipient audit report of Federal funds.

**Recommendation**

We recommend the DMA develop and implement a system to properly monitor subrecipient activities to adequately comply with OMB Circular A-133 subrecipient monitoring compliance requirements.

In addition to procedures already in place, the monitoring and tracking system should contain the following at a minimum:

1. Monitor the activities of subrecipients as necessary to ensure federal awards are used in compliance with laws, regulations, and grant agreements;
2. Ensure subrecipients expending \$300,000 or more in federal awards during the subrecipient's fiscal year have met the audit requirements for compliance with receiving the federal award;

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-MIL2-37: The Department Of Military Affairs Should Implement A System To Properly Monitor Subrecipient Activities To Comply With OMB Circular A-133 Compliance Requirements (Continued)**

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**Recommendation (Continued)**

3. Issue a management decision on audit findings within six (6) months after receipt of the subrecipient's audit report and ensure the subrecipient takes appropriate corrective action.

**Management's Response and Corrective Action Plan**

*We agree with the findings of inadequate monitoring of sub-recipients of federal awards through our agency. As a result of numerous Presidential Disaster Declarations and their associated activities as well as the limited amount of staffing assigned to our agency, we have been unable to meet the monitoring compliance requirements of OMB Circular A-133.*

*If proper staffing were available and assigned, our intent would be to commit our agency to fulfilling this requirement and plan to take the following steps to resolve these findings and improve our performance in the areas listed as deficient:*

1. *Inform sub-recipients of their audit requirement in writing when the federal award is made.*
2. *A form will be developed and sent to each sub-recipient at the end of the sub-recipient's fiscal year reminding them of the audit requirement and requiring them to inform Department of Military Affairs/KyEM of the status of their compliance with applicable audit requirements and any deficiencies noted in their audits relating to federal funds provided by KyEM.*
3. *If deficiencies or irregularities are noted in the audit reports, the sub-recipient will be contacted by an employee of the Department for Military Affairs and asked to explain the status of its effort to correct them.*
4. *Monitor the activities of sub-recipients as necessary to ensure that Federal awards are used in compliance with laws and regulations.*
5. *Ensure that sub-recipients have met all of the audit requirements for compliance with receiving federal funds.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-MIL2-37: The Department Of Military Affairs Should Implement A System To Properly Monitor Subrecipient Activities To Comply With OMB Circular A-133 Compliance Requirements (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

6. *Issue a management decision on audit findings within six months after receipt of the sub-recipient's audit report and ensure that the sub-recipient takes appropriate corrective action.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-TC11-38: The Transportation Cabinet Should Obtain Proper Federal Highway Administration Approval Prior To Starting Eligible Federal Assistance Projects**

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State Organization: Transportation Cabinet

Federal Program: CFDA 20.205-Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Special Tests and Provisions

Amount of Questioned Cost: None

The Transportation Cabinet did not obtain proper FHWA approval prior to granting authority to advertise or prior to the actual newspaper advertisement date for construction projects. During our testing of construction expenditures, two (2) of the 25 projects tested did not have FHWA approval prior to the TC granting authority to advertise or prior to the newspaper advertisement date.

Per the Catalog of Federal Domestic Assistance for CFDA #20.205, “[t]he FHWA approval constitutes a commitment to pay the Federal share of the project cost.” In proceeding without this approval, projects not meeting federal guidelines may have to be the financial responsibility of the Commonwealth.

Project activities started without the proper FHWA approval is not in compliance with OMB Circular A-133 or the Code of Federal Regulations.

OMB Circular A-133 states:

Construction projects administered under standard procedures cannot be advertised nor force account work commenced until FHWA: (1) approves the plans, specifications, and estimates; and (2) authorizes the State DOT to advertise for bids or approves the force account work (23 CFR sections 630.205(c), 635.211(a), and 635.309). Construction cannot begin until after FHWA concurs in the contract award (23 CFR section 635.114). This requirement does not apply to construction projects administered by the State DOT under 23 USC 106(c) which allow the State DOT to assume the responsibilities for design, plans, specifications, estimates, contract awards, and inspection of progress (23 USC 106 (c)).

**Recommendation**

We recommend that the TC obtain proper FHWA approvals prior to granting the authority to advertise and before the advertisement date for the projects.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-TC11-38: The Transportation Cabinet Should Obtain Proper Federal Highway Administration Approval Prior To Starting Eligible Federal Assistance Projects (Continued)**

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**Management's Response and Corrective Action Plan**

*Policies have been put in place to require all necessary information be supplied two weeks prior to the advertised date. This requirement was effective with the May 14, 2004 letting. Any project which does not meet this criteria is to be pulled from the letting until all documentation is in place.*



**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-TC12-39: The Transportation Cabinet Should Maintain Documentation That Supports Figures Reported In The Annual Federal Highway Administration Statistics Report**

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State Organization: Transportation Cabinet

Federal Program: CFDA 20.205 – Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Cost: None

During our audit testing of the FY 03 Annual FHWA Statistics Report, we noted that amounts reported for Acquisition and Relocation Expenses were not reported accurately based on agency provided criteria. Further, it cannot be determined if state matching funds are included in the statistical report. FHWA prefers the Transportation Cabinet include the state match.

We also noted that last resort housing payments were not subtracted from replacement housing payments for the report as the instructions state.

Similar problems were noted last year. The TC has begun keeping ledgers of all payments made for acquisitions and condemnations. The ledgers represent the actual dollars spent, rather than only the amount actually billed to FHWA. According to our reconciliation to MARS, acquisition expenses were understated by \$5,454,439 and relocation expenses were understated by \$356,668.

Also, \$28,395 in last resort housing payments was not subtracted from Replacement Housing Payments (RHP) on the report. This led to the overstatement of the line item “RHP for Owners.”

The instructions for the consolidated Statistical Reporting Form states, “Last Resort payment figures should only report the number of cases where payments exceeded the maximum supplement, and the dollar amount of that excess. The maximum supplement amount should be reflected on the lines of either the Rental Supplement, Down Payments, or RHP for Owners . . .”

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-TC12-39: The Transportation Cabinet Should Maintain Documentation That Supports Figures Reported In The Annual Federal Highway Administration Statistics Report (Continued)**

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**Recommendation**

We recommend the Division of Right of Way and Utilities develop policies and procedures for submitting a report that will be reconciled to MARS on a quarterly basis and to perform comparisons as planned. Variances found during the comparisons and the resolution of those variances should be documented. Backup documentation for the figures reported on the Annual Statistical Report should be maintained for audit purposes. Relocation figures, particularly last resort housing costs, should be reported as required by the instructions that accompany the report.

**Management's Response and Corrective Action Plan**

*The expenditures reported on the annual FHWA Statistics Report contain the actual dollars spent on acquiring right of way for the Cabinet. The figures reported do not represent any amount actually billed to FHWA.*

*The following corrective actions will be implemented immediately to ensure the accuracy of the report:*

- 1. A new reporting category will be developed in relocation to ensure the breakdown of last resort housing costs and the replacement housing payments are reported accurately.*
- 2. Due to the fact that we are halfway through the current federal fiscal year, a query will be done from MARS MRDB for each month of the current fiscal year that has passed. A review will be done on the expenditures to ensure accuracy. Department personnel will review relocation. This monthly review will continue through the remainder of the current federal fiscal year (September 30, 2004). Any corrections will be documented.*
- 3. All backup documentation (paper and/or electronic) will be retained for auditing purposes.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-CWD10-40: The Department For Training And ReEmployment  
Should Implement Controls Over Monitoring Procedures To Ensure Compliance**

State Organization: Cabinet For Workforce Development  
Federal Program: CFDA 17.255 – Workforce Investment Act  
Federal Agency: U.S. Department of Labor  
Pass-Through Agency: Not Applicable  
Compliance Area: Subrecipient Monitoring  
Amount of Questioned Costs: None

During the FY 03 audit, we tested the audit log maintained by the Department for Training and ReEmployment (DTR) to track subrecipient monitoring related to the required audits of subrecipients. During this review, the auditor noted the following:

- DTR did not obtain subrecipient audit reports in a timely manner to comply with federal regulations.
- DTR did not resolve subrecipient audit findings timely. Two (2) subrecipient audit reports contained findings related to the Workforce Investment Act (WIA) program, which have yet to be fully resolved. Furthermore, the eligibility finding for Lake Cumberland Area Development District (ADD) initially occurred in the FY 01 audit. Lake Cumberland ADD submitted a corrective action plan in December 2003; however, questioned costs related to the finding have not been resolved. DTR also failed to issue an initial determination upon receipt of the corrective action plan from the Bluegrass ADD. DTR has not followed up on the corrective action plan to resolve the findings. The final determination reported no findings or questioned costs for either ADD.
- Agency records were not reconciled to the subrecipients' audited financial statements for several Local Workforce Investment Areas. Amended DTR-38s (Quarterly Cash Reconciliations) were submitted to agree to the audited financial statements. However, there was no support or explanation for the adjustments.

These findings relate to the local area FY 02 OMB Circular A-133 audits; however, DTR has made improvements related to future audits.

- The receipt of the audit reports in an untimely manner delays the entire resolution process. It also increases the likelihood that subrecipient weaknesses noted in the audit continue for longer periods of time since they are not being addressed.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-CWD10-40: The Department For Training And ReEmployment  
Should Implement Controls Over Monitoring Procedures To Ensure Compliance  
(Continued)**

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- When reports submitted to grantors are not reconciled, it can lead to the potential that federal reporting does not agree to the financial statements on which an opinion has been given.

According to OMB Circular A-133, the funding agency should be sent a copy of the audit report within the *earlier* of 30 days after [the subrecipient's] receipt of the auditor's report(s), or nine (9) months after the end of the audit period. This requirement is also outlined in DTR's Audit Resolution Guide. This requirement is in effect for fiscal years beginning after June 30, 1998. [OMB Circular A-133 Subpart C, Sec. 320 (a)]

The WIA regulations state: "The Governor is responsible for resolving findings that arise from the State's monitoring reviews, investigations and audits (including OMB Circular A-133 audits) of subrecipients." [20 CFR 667.500 (a) (1)]

Further, according to OMB Circular A-133, pass-through entities are responsible for making the management decision on audit findings of subrecipients within six (6) months after receipt of the audit report. Corrective action should also be initiated within six (6) months after receipt of the audit report. [OMB Circular A-133 Subpart D Sec .400 (d)(5)]

**Recommendation**

The DTR should continue to improve their monitoring procedures to ensure compliance with the WIA regulations, OMB Circular A-133, and the DTR guidelines regarding audit resolutions of subrecipients.

We recommend that the DTR implement procedures to ensure timely management decisions on audit and monitoring findings and require subrecipients to initiate corrective action on deficiencies identified in audits and subrecipient monitoring within six (6) months after receipt of the audit report.

We also recommend that agency records be reconciled to the audited financial statements. All supporting documentation should be maintained for any differences, such as auditor adjustments, accrued revenue, accrued expenses, etc.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-CWD10-40: The Department For Training And ReEmployment  
Should Implement Controls Over Monitoring Procedures To Ensure Compliance  
(Continued)**

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**Management's Response and Corrective Action Plan**

*DTR agrees with this finding and will implement procedures to ensure timely management decisions on audit and monitoring findings, and require subrecipients to initiate corrective action on deficiencies identified in audits and subrecipient monitoring within six months after receipt of audit reports in future periods.*

*DTR will immediately initiate our audit finding resolution process for the Lake Cumberland ADD and Bluegrass ADD audits for FY 2002 and continue to follow-up on the Lake Cumberland ADD's resolution efforts of the eligibility issue finding disclosed in their FY 2001 audit.*

*DTR also agrees to reconcile agency records to the audited financial statements and maintain supporting documentation for any differences such as auditor adjustments, accrued revenue, accrued expenses, etc.*

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-CWD11-41: The Department For Training And ReEmployment  
Should Implement Formal Procedures To Ensure Accurate Federal Reporting**

State Organization: Cabinet For Workforce Development  
Federal Program: CFDA 17.255 – Workforce Investment Act  
Federal Agency: U.S. Department of Labor  
Pass-Through Agency: Not Applicable  
Compliance Area: Reporting  
Amount of Questioned Costs: None

The U.S. Department of Labor (DOL) required a closeout certification for the WIA expenditures carried forward from the Job Training Partnership Act (JTPA) to be submitted by March 2003. The WIA Financial Status Reports for Program Year 1998 and 1999 were not properly supported. The total expenditures reported for each program year do not agree to the total funds carried forward from the JTPA program as certified to DOL.

We were able to reconcile federal reports to MARS for grants reported the quarter ending March 31, 2003 and after. However, there were expenditures reported in MARS that lacked a reporting category or activity code and expenditures that were miscoded; therefore, the funding source could not be properly identified.

DTR has not developed written procedures for the preparation, review, and approval of federal reports. As a result, it is difficult for someone other than the preparer to recreate the amounts reported.

- Without supporting documentation, DOL could be unable to determine if WIA transition funds were properly closed out.
- When there are numerous accounts, it can result in miscoded expenditures that may not be reported correctly. Also, it can result in inconsistent categorization of expenditures for grant reporting purposes.
- When written procedures are not in place it can result in federal reporting which is not consistent or easy to follow. When federal reports are not reviewed, errors can go undetected and uncorrected before submission.

Proper internal controls dictate that accurate and reliable information be maintained after preparing and transmitting federal reports. Reports should be adequately supported with valid and accurate documentation.

**COMMONWEALTH OF KENTUCKY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

**SECTION 3 – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**FINDING 03-CWD11-41: The Department For Training And ReEmployment  
Should Implement Formal Procedures To Ensure Accurate Federal Reporting  
(Continued)**

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A complete policies and procedures manual will provide a structure for preparing federal reports and enable someone to review the reports for accuracy.

**Recommendation**

We recommend DTR continue to improve the federal reporting process. Proper supporting documentation should be maintained with all federal reports and reconciled to MARS quarterly to ensure accuracy. We recommend the agency fully utilize the capabilities of MARS for tracking expenditures for each funding stream and develop internal controls to prevent miscoding of expenditures. We also recommend DTR develop written procedures for the preparation, review, and approval of federal reports.

**Management's Response and Corrective Action Plan**

*Although DTR has implemented many improvements in the utilization of MARS to support the federal financial reports, we agree that implementing the recommendations mentioned above would further improve our processes. DTR will develop and implement written procedures for the preparation, review, and approval of federal reports beginning with the period ending March 31, 2004. DTR will develop and implement internal controls to prevent miscoding of expenditures. DTR will ensure that adequate supporting documentation for federal reports is maintained and reconciled to MARS on a quarterly basis to ensure accuracy.*

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**



**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions</u></b>					
<i>(1) Audit findings that have been fully corrected:</i>					
FY 02	02-KAP1-1	The Kentucky Access Program Should Ensure The Operating Account Is Properly Collateralized	NA	0	Resolved during FY 03.
FY 02	02-CFC1-2	The Cabinet For Families And Children Should Strengthen Security Surrounding Administrator Accounts	NA	0	Resolved during FY 03.
FY 02	02-FAC1-4	The Finance And Administration Cabinet Should Closely Monitor The Progress Of The Disparity Study Relating To Set-Aside Laws	NA	0	Resolved during FY 03.
FY 02	02-FAC5-8	The Finance And Administration Cabinet Should Work With American Management Systems To Strengthen Logical Security Measures Over The Management Administrative Reporting System And The Management Reporting Database	NA	0	Resolved during FY 03.
FY02	02-FAC6-9	The Finance And Administration Cabinet Should Work With The Governor's Office For Technology To Ensure The Security Log Report Is Generated, Recoverable, And Effectively Monitored	NA	0	Resolved during FY 03.
FY02	02-FAC8-11	The Finance And Administration Cabinet Should Strengthen The Security Of Administrator Accounts	NA	0	Resolved during FY 03.
FY02	02-FAC9-12	The Finance And Administration Cabinet Should Ensure That All Open Ports On Agency Machines Have A Business-Related Purpose	NA	0	Due to improvements, this finding is downgraded to an other matter for FY 03. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 01	01-FAC6-7	The Office Of Technical Services Should Improve Security Of The Servers Within The Local Area Networks For Finance And Administration Cabinet	NA	0	Resolved during FY 03.
FY 01	01-FAC7-8	The Finance And Administration Cabinet Should Implement Policies And Procedures To Ensure Compliance With Applicable Small Or Small Minority Business Set-Aside Laws	NA	0	Resolved during FY 03.
FY 99	99-FAC-13	The Finance And Administration Cabinet Should Implement Policies And Procedures Relating To Small Or Small Minority Business Set-Aside Laws	NA	0	Resolved during FY 03.
FY 02	02-CHS1-13	The Cabinet For Health Services Should Strengthen The Security Of System Administrator Accounts	NA	0	Resolved during FY 03.
FY 02	02-CHS12-36	The Division of Program Integrity Has A Large Outstanding Balance Of Accounts Receivable For The Drug Rebate Program	93.778	0	Due to improvements, this finding is downgraded to an other matter for FY 03. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 02	02-CHS13-37	The Division Of Program Integrity Does Not Track Interest Due On Outstanding Drug Rebate Accounts	93.778	0	Due to improvements, this finding is downgraded to an other matter for FY 03. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 02	02-CHS14-38	The Division Of Managed Care Does Not Maintain Records Of Complaints And Grievances	93.778	0	Resolved during FY 03.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 01	01-CHS9-42	The Drug Rebate Program Should Be More Involved In The Dispute Resolution Program In Order To Collect More Money	93.778	0	Due to improvements, this finding is downgraded to an other matter for FY 03. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 00	00-CHS-18	The Department For Medicaid Services Should Improve Claims Processing, Including The Dispute Resolution Process With Drug Rebate Manufacturers	93.778	0	Due to improvements, this finding is downgraded to an other matter for FY 03. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 99	99-CHS-36	The Department For Medicaid Services Should Improve The Controls Over Drug Rebate Billings, Collections And Recordings	93.778	0	Due to improvements, this finding is downgraded to an other matter for FY 03. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 02	02-PERS1-16	The Personnel Cabinet Should Provide Adequate Logical Security Controls For Access To The Unified Payroll And Personnel System	NA	0	Resolved during FY 03.
FY 01	01-PERS1-17	The Personnel Cabinet Should Improve Security Controls For Uniform Payroll And Personnel System Logical Access	NA	0	Resolved during FY 03.
FY 98	98-PERS-9	The Personnel Cabinet Should Implement Adequate Logical Access Security For The Unified Personnel And Payroll System	NA	0	Resolved during FY 03.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 02	02-CPE1-44	The Council On Postsecondary Education Should Implement Additional Procedures To Ensure Required Information For Eisenhower Professional Development State Grants Is Obtained And Reviewed In A Timely Manner	84.281	0	Resolved during FY 03.
FY 02	02-CPE2-45	The Council On Postsecondary Education Should Implement Additional Procedures To Ensure Required Information For Gaining Early Awareness And Readiness For Undergraduate Programs Is Obtained In A Timely Manner	84.334	0	Resolved during FY 03.
FY 01	01-CPE2-48	The Council On Postsecondary Education Should Implement Additional Follow Up Procedures To Ensure That Required Information Is Requested If Not Received In A Timely Manner	84.281	0	Resolved during FY 03.
FY 02	02-REV5-20	The Kentucky Revenue Cabinet Should Ensure All Open Ports On Agency Machines Have A Business-Related Purpose	NA	0	Due to improvements, this finding is downgraded to an other matter for FY 03. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 02	02-KST1-22	The Office Of The Kentucky State Treasurer Should Ensure Significant Accounting Functions Are Adequately Separated To Reduce The Risk Of Errors	NA	0	Resolved during FY 03.
FY 02	02-CWD1-23	The Division Of Unemployment Insurance Is Not Reviewing Accounts And Declaring Them Uncollectible	NA	0	Resolved during FY 03.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 02	02-CWD3-24	The Cabinet For Workforce Development Should Strengthen Controls Over Estimation Of Accounts Payable	NA	0	Resolved during FY 03.
FY 02	02-CWD11-50	The Department For Training And ReEmployment Did Not Reconcile Subrecipient Expenditures To MARS	17.255 17.258 17.259 17.260	0	Resolved during FY 03.
FY 02	02-CWD13-52	The Division Of Unemployment Insurance Should Ensure Federal Reports Are Supported By Accurate And Reliable Data	17.225	0	Resolved during FY 03.
FY 02	02-CWD14-53	The Division Of Unemployment Insurance Should Implement Procedures To Ensure The Accuracy And Timeliness Of The IRS 940 Federal Unemployment Tax Administration Certification	17.225	0	Resolved during FY 03.
FY 01	01-CWD2-22	The Division Of Unemployment Insurance Allowance For Uncollectible Accounts Was Not Updated For Current Year Actions	NA	0	Resolved during FY 03.
FY 01	01-CWD10-53	The Division Of Unemployment Insurance Is Not Reconciling Accounts Receivable To Ensure Federal Reports Are Accurate	17.225	0	Resolved during FY 03.
FY 01	01-CWD11-54	The Division Of Unemployment Insurance Has Not Performed The 1999 Certification Of Employer Contributions	17.225	0	Resolved during FY 03.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 02	02-CFC2-3	The Cabinet For Families And Children's Password Policy Should Be Consistently Applied To All Local Area Network Servers	NA	0	Specific issues improved from the prior year, but additional occurrences were identified for certain servers so the same general issues existed.  See 03-CFC1-1.
FY 02	02-CFC12-33	The Cabinet For Families And Children Should Develop A Policy And Procedures Manual To Ensure Subrecipient Monitoring Is Properly Performed	17.253 93.563 93.575	0	CFC has made progress toward complying with audit recommendations; however, exceptions were still noted.  See 03-CFC6-28.
FY 02	02-CFC14-34	The Cabinet For Families And Children Should Monitor Cases Closely So An Ineligible Recipient Does Not Receive Additional Months Of Benefits	93.558	\$2,616	FY 03 testing indicated this weakness still exists.  See 03-CFC7-29.
FY 02	02-CFC15-35	The Cabinet For Families And Children Should Maintain And Produce Records To Adequately Support Expenditures	93.558	0	FY 03 testing revealed missing case files and documentation. CFC has made significant improvement, but weaknesses still exist.  See 03-CFC8-30.
FY 01	01-CFC1-1	The Cabinet For Families And Children Should Improve Local Area Network Server Security And Consistently Apply Policies To All Servers	NA	0	Specific issues improved from the prior year, but additional occurrences were identified for certain servers so the same general issues existed.  See 03-CFC1-1.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(2) Audit findings not corrected or partially corrected (Continued):</i>					
FY 01	01-CFC2-36	The Cabinet For Families And Children Should Maintain And Produce Records To Adequately Support Expenditures	93.558	0	FY 03 testing revealed missing case files and documentation. CFC has made significant improvement, but weaknesses still exist.  See 03-CFC8-30.
FY 01	01-CFC4-38	The Cabinet For Families And Children Should Develop A Policies And Procedures Manual To Ensure Subrecipient Monitoring Is Properly Performed	17.253 93.558 93.563 93.568 93.575 93.596	0	CFC has made progress toward complying with audit recommendations; however, exceptions were still noted.  See 03-CFC6-28.
FY 00	00-CFC-12	The Cabinet For Families And Children Should Impose Sanctions On Subrecipients Who Fail To Meet Audit Requirements Set Forth By OMB Circular A-133	93.558 93.563 93.575 93.596	0	CFC has made progress toward complying with audit recommendations; however, exceptions were still noted.  See 03-CFC6-28.
FY 02	02-FAC2-5	The Finance And Administration Cabinet Should Ensure Consistent Classification And Categorization Of Investments In The Cash And Investment Note	NA	0	The cash and investment note preparation process has improved, but improvements are still needed in the classification and categorization areas.  See 03-FAC1-3.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<b><i>(2) Audit findings not corrected or partially corrected (Continued):</i></b>					
FY 02	02-FAC3-6	The Finance And Administration Cabinet Should Develop And Consistently Apply Formal Change Management Control Procedures For The Commonwealth's Cash And Investment Statistical Analysis System Programs	NA	0	Although OFM has taken steps in attempt to improve a couple of the issues noted within this comment, weaknesses still reside. Further, the comment has been expanded and renamed to incorporate additional system development life cycle issues noted for FY 03.  See 03-FAC6-8.
FY 02	02-FAC4-7	The Office Of Financial Management Should Improve Segregation Of Duty Controls	NA	0	Although OFM has taken action in an attempt to improve a couple of the issues noted within this comment, these actions are not deemed sufficient. Issues were again noted with OFM's segregation of duty controls for FY 03.  See 03-FAC7-9.
FY02	02-FAC7-10	The Finance And Administration Cabinet Should Ensure All User Accounts On Its Agency Servers Are Necessary	NA	0	Exceptions were noted during testing for FY 03 with some of the same machines and some new ones.  See 03-FAC3-5.
FY 01	01-FAC2-3	The Finance And Administration Cabinet Should Improve Controls Over Preparation Of The Cash And Investment Note	NA	0	The cash and investment note preparation process has improved, but improvements are still needed in the classification and categorization areas.  See 03-FAC1-3.



**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(2) Audit findings not corrected or partially corrected (Continued):</i>					
FY 01	01-FAC3-4	The Office Of Financial Management Should Improve Control Procedures Over Modifications To System Programs	NA	0	See 03-FAC6-8.
FY 00	00-FAC-6	The Office Of Financial Management Should Improve Control Procedures Over Modifications To System Programs	NA	0	See 03-FAC6-8.
FY 02	02-CHS2-14	The Vital Statistics Branch Should Improve Controls Over Assets And Separate Work Tasks	NA	0	Significant progress has been made, but one area still needs improvement.  See 03-CHS2-11.
FY 02	02-CHS3-15	The Vital Statistics Branch Should Take Steps To Reduce The Identity Theft Risks	NA	0	The CHS continues to seek legislation.  See 03-CHS1-12.
FY 01	01-CHS4-13	The Vital Statistics Branch Should Improve Security Over Assets And Segregate Job Duties	NA	0	Significant progress has been made, but one area still needs improvement.  See 03-CHS2-11.
FY 01	01-CHS6-15	The Vital Statistics Branch Should Take Steps To Prevent Identity Theft	NA	0	The CHS continues to seek legislation.  See 03-CHS1-12.
FY 02	02-JUST1-39	The Justice Cabinet Should Develop An Indirect Cost Plan And Submit It To The Cognizant Federal Agency For Approval	16.575 16.579 16.588	0	See 03-JUST1-32 and 03-JUST5-36.
FY 02	02-JUST2-40	The Justice Cabinet Should Develop Written Subrecipient Monitoring Policies And Procedures To Ensure Subrecipient Monitoring Is Properly Performed And Documented	16.575 16.579 16.588	0	Subrecipient monitoring procedures included in updated policies and procedures manual during FY 03.  See 03-JUST2-33.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(2) Audit findings not corrected or partially corrected (Continued):</i>					
FY 02	02-JUST3-41	The Justice Cabinet Should Perform Sufficient Subrecipient Monitoring Activities To Ensure Subrecipients Expending More Than \$300,000 In Federal Awards Receive OMB Circular A-133 Audits	16.575 16.579 16.588	0	See 03-JUST3-34.
FY 02	02-JUST4-42	The Justice Cabinet Should Prepare Quarterly Financial Status Reports That Are Supported By Adequate Documentation	16.575 16.579 16.588	0	See 03-JUST4-35.
FY 02	02-MIL1-43	The Department Of Military Affairs Should Ensure Subrecipient Monitoring Is Properly Performed	83.544	0	Attempts at monitoring and tracking are being made. However, not all required audits were submitted.  See 03-MIL2-37.
FY 01	01-MIL1-46	The Department Of Military Affairs Should Ensure Subrecipients Meet OMB Circular A-133 Audit Requirements	83.544	0	Attempts at monitoring and tracking are being made. However, not all required audits were submitted.  See 03-MIL2-37.
FY 97	97-Military Affairs-50	The Department Of Military Affairs Should Strengthen Procedures For Monitoring Subrecipients	83.544	\$62,500	Attempts at monitoring and tracking are being made. However, not all required audits were submitted.  See 03-MIL2-37.
FY 00				(34,747)	
FY 02				(27,743)	
Total Questioned Costs				<u>\$0</u>	
FY 02	02-REV1-17	The Kentucky Revenue Cabinet Should Ensure Confidential Taxpayer Information Is Protected And Preserved As Required By Statute	NA	0	See 03-REV1-13.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(2) Audit findings not corrected or partially corrected (Continued):</i>					
FY 02	02-REV2-18	The Kentucky Revenue Cabinet Should Update The Sales Tax Database And Automate Processing Of Accelerated Tax Returns	NA	0	See 03-REV2-14.
FY 02	02-REV4-19	The Kentucky Revenue Cabinet Should Strengthen The Security Surrounding Administrator Accounts	NA	0	See 03-REV3-15.
FY 02	02-REV6-21	The Kentucky Revenue Cabinet Should Ensure All User Accounts On The Agency Servers Are Necessary	NA	0	See 03-REV4-16.
FY 01	01-REV1-18	The Revenue Cabinet Should Update The Sales Tax Database And Automate Processing Of Accelerated Tax Returns	NA	0	See 03-REV2-14.
FY 01	01-REV3-19	The Revenue Cabinet Should Have A System In Place To Reconcile Critical Information	NA	0	See 03-REV5-17.
FY 02	02-TC2-46	The Transportation Cabinet Should Develop Internal Controls To Ensure Accurate Presentation Of The Annual Federal Highway Administration Statistics Report	20.205	0	See 03-TC12-39.
FY 02	02-TC3-47	The Transportation Cabinet Should Ensure The Annual Federal Highway Administration Report Is Compiled In Compliance With Federal Guidelines	20.205	0	See 03-TC12-39.
FY 02	02-TC5-49	The Transportation Cabinet Should Obtain Federal Highway Administration Approvals Prior To Granting Authority To Advertise And Before Actually Advertising For Projects	20.205	0	See 03-TC11-38.
FY02	02-CWD4-25	The Cabinet For Workforce Development Should Strengthen The Security Of Administrator Accounts	NA	0	See 03-CWD3-27.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions (Continued)</u></b>					
<i>(2) Audit findings not corrected or partially corrected (Continued):</i>					
FY 02	02-CWD12-51	The Department For Training And ReEmployment Should Implement Additional Procedures To Ensure Subrecipient Findings Are Followed Up On In A Timely Manner	17.255 17.258 17.259 17.260	0	See 03-CWD11-41.
FY 01	01-CWD3-23	The Cabinet For Workforce Development Should Improve Local Area Network Server Security And Consistently Apply Policies To All Servers	NA	0	See 03-CWD3-27.
<i>(3) Corrective action taken is significantly different from corrective action previously reported:</i>					
No findings for this section.					
<i>(4) Audit finding is no longer valid or does not warrant further action:</i>					
FY 98	98-CFC-27	The Cabinet For Families And Children Should Maintain Records To Support Payments To Participants In The Kentucky Works Program	93.558	\$0 777 (777)	Questioned costs were resolved in FY 01.
FY 97					
FY 01					
		Total Questioned Costs		<u>\$0</u>	
FY 02	02-TC4-48	The Transportation Cabinet Should Ensure Federal Expenditures Are Made Only For Allowable Costs	20.205	\$1,565	The agency decided it would not be cost efficient to pursue this amount through legal channels.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Material Weaknesses/Noncompliances</u></b>					
<i>(1) Audit findings that have been fully corrected:</i>					
FY 02	02-CPE3-26	The Council On Postsecondary Education Should Implement Additional Procedures To Ensure Information Required For The Professional Education Preparation Program Is Requested If Not Received In A Timely Manner	NA	0	Resolved during FY 03.
FY 02	02-CPE4-27	The Council On Postsecondary Education Should Consider Additional Procedures To Ensure Information Required For The Minority Student College Preparation Program Is Received In A Timely Manner	NA	0	Resolved during FY 03.
FY 02	02-CPE5-28	The Council On Postsecondary Education Should Implement Additional Procedures To Ensure Information Required For The Kentucky Educational Excellence Scholarship Program Is Requested If Not Received In A Timely Manner	NA	0	Resolved during FY 03.
FY 02	02-CPE6-29	The Council On Postsecondary Education Should Investigate Alternatives To Address The Apparent Inconsistency Between The Current Council Guidelines And The Current Provision Of KRS 164.7919(1)(c)	NA	0	Resolved during FY 03.
FY 02	02-CPE7-30	The Council On Postsecondary Education Should Revise The Guidelines Applicable To The Regional University Excellence Trust Fund	NA	0	Resolved during FY 03.
FY 01	01-CPE3-27	The Council On Postsecondary Education Should Investigate Alternatives To Address The Apparent Inconsistency Between The Current Council Guidelines And The Current Provisions Of KRS 164.7919(1)(c)	NA	0	Resolved during FY 03.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Material Weaknesses/Noncompliances (Continued)</u></b>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 01	01-CPE4-28	The Council On Postsecondary Education Should Revise The Guidelines Applicable To The Regional University Excellence Trust Fund To More Clearly Define The Amount Of Matching That Will Be Permitted In The Areas Of Arts And Humanities	NA	0	Resolved during FY 03.
FY 01	01-CPE5-29	The Council On Postsecondary Education Should Implement Additional Procedures To Ensure That The Required Information Is Requested If Not Received In A Timely Manner	NA	0	Resolved during FY 03.
FY 99	99-CWD-30	The Division of Unemployment Insurance Should Ensure Computer Accounting Systems Are Operating Effectively And Amounts Reported From Those Systems Can Be Supported	NA	0	Resolved during FY 03.
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 02	02-REV3-31	The Kentucky Revenue Cabinet Should Have A System In Place To Reconcile Critical Information	NA	0	The reconciliation is expected to be operational in FY 04. Due to improvements, this finding is downgraded to a reportable condition for FY 03.  See 03-REV5-17.

**COMMONWEALTH OF KENTUCKY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
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**Material Weaknesses/Noncompliances (Continued)**

***(2) Audit findings not corrected or partially corrected (Continued):***

FY 02	02-CWD2-32	The Division Of Unemployment Insurance Should Have A Computer System In Place To Adequately Maintain Employer Accounts	NA	0	Due to improvements, this finding is downgraded to a reportable condition for FY 03.  See 03-CWD2-26.
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***(3) Corrective action taken is significantly different from corrective action previously reported:***

No findings for this section.

***(4) Audit finding is no longer valid or does not warrant further action:***

No findings for this section.

## **APPENDICES**



**COMMONWEALTH OF KENTUCKY  
APPENDIX 1  
FOR THE YEAR ENDED JUNE 30, 2003**

List Of State Organizations Audited As Part Of The  
Statewide Single Audit Of The Commonwealth

The list includes agencies receiving only financial statement audits used for preparing the Commonwealth's CAFR. CPA reports are available upon request to the respective audited agency.

**STATE ORGANIZATIONS AUDITED BY CERTIFIED PUBLIC ACCOUNTING  
FIRMS AND INCLUDED IN SSWAK:**

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Kentucky Affordable Prepaid Tuition  
Kentucky Center for the Arts  
Bluegrass State Skills Corporation  
Eastern Kentucky Exposition Center Corporation  
Kentucky Economic Development Finance Authority  
Kentucky Educational Savings Plan Trust  
Kentucky Educational Television Authority  
Kentucky Higher Education Assistance Authority  
Kentucky Higher Education Student Loan Corporation  
Kentucky Horse Park  
Kentucky Housing Corporation  
Kentucky Infrastructure Authority  
Judicial Form Retirement System  
Kentucky Local Correctional Facilities Construction Authority  
Kentucky Lottery Corporation  
Office of the Petroleum Storage Tank Environmental Assurance Fund  
Council on Postsecondary Education  
Kentucky Public Employees' Deferred Compensation Authority  
Kentucky Retirement Systems  
Kentucky River Authority  
Kentucky State Fair Board  
Kentucky Teachers' Retirement Systems  
Turnpike Authority of Kentucky  
Kentucky Worker's Compensation Funding Commission  
Kentucky Worker's Compensation Special Fund, Coal Workers' Pneumoconiosis Fund  
(functions of the Labor Cabinet), and Uninsured Employers' Fund (function of the Office  
of the Attorney General)

**COMMONWEALTH OF KENTUCKY  
APPENDIX 1  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of State Organizations Audited As Part Of The Statewide Single Audit Of The Commonwealth (Continued)

**STATE ORGANIZATIONS AUDITED BY CERTIFIED PUBLIC ACCOUNTING FIRMS AND NOT INCLUDED IN SSWAK, EXCEPT FOR EXPENDITURE AMOUNTS IN THE OPINION LETTER:**

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Eastern Kentucky University\*  
Kentucky Community Technical College System  
Kentucky State University\*  
Morehead State University  
Murray State University  
Northern Kentucky University  
University of Kentucky  
University of Louisville  
Western Kentucky University

\* The Eastern Kentucky University and Kentucky State University audit reports on the basic financial statements were not available at December 23, 2003; however, the OMB Circular A-133 audit reports were available March 8, 2004.

**STATE ORGANIZATIONS AUDITED BY THE AUDITOR OF PUBLIC ACCOUNTS:**

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Kentucky Access (Financial Statement Only)  
Department of Education  
Cabinet for Families and Children  
Finance and Administration Cabinet  
Cabinet for Health Services  
Justice Cabinet (Federal Awards Only)  
Department for Local Government (Federal Awards Only)  
Department of Military Affairs (Federal Awards Only)  
Personnel Cabinet – Risk Management Funds (Financial Statement Only)  
Kentucky Revenue Cabinet (Financial Statement Only)  
Transportation Cabinet  
Office of the Kentucky State Treasurer - Cash Functions (Financial Statement Only)  
Department of Parks (Financial Statements Only)  
Cabinet for Workforce Development

**COMMONWEALTH OF KENTUCKY  
APPENDIX 2  
FOR THE YEAR ENDED JUNE 30, 2003**

List Of State Organization Contacts

If additional copies of the statewide single audit are required, please contact Greg Giesler, Open Records Administrator, with the APA's office at (502) 573-0050 or [ggiesler@kyauditor.net](mailto:ggiesler@kyauditor.net). If copies of the CAFR for the FY 03 are required, please contact Robbie Rudolph, Finance and Administration Cabinet Secretary, at (502) 564-4240.

The following is a list of individuals by state organizations to contact regarding findings in the Schedule of Findings and Questioned Costs or the Summary Schedule of Prior Audit Findings.

<b>State Organization</b>	<b>Contact</b>
Kentucky Access Program	Frederick Nelson, JD, Director Division of Kentucky Access Department of Insurance P.O. Box 1380 Frankfort, KY 40602-1380 Phone: (502) 573-1026
Cabinet for Families and Children	Kelli Hill, Manager Division of Financial Management Cabinet for Families and Children 275 East Main Street 4C-C Frankfort, KY 40601 Phone (502) 564-2250 ext. 4336
Finance and Administration Cabinet	Stuart Weatherford, Director Division of Statewide Accounting Services Finance and Administration Cabinet Capitol Annex, Room 484 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-7750  Ed Ross, Controller Office of the Controller Finance and Administration Cabinet Capitol Annex, Room 393 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-2210

**COMMONWEALTH OF KENTUCKY  
APPENDIX 2  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of State Organization Contacts (Continued)

<b>State Organization</b>	<b>Contact</b>
Finance and Administration Cabinet (Continued)	George Burgess, Executive Director Office of Financial Management Finance and Administration Cabinet Capitol Annex, Room 261 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-2924
Cabinet for Health Services	Miles Murphy, Assistant Director Division of Policy and Financial Management Cabinet for Health Services 275 East Main Street 5W-C Frankfort, KY 40601 Phone (502) 564-8890 Ext. 3374
Justice Cabinet-Office of the Secretary	Tanya Dickinson, Branch Manager Division of Grants Management Justice Cabinet 403 Wapping St Frankfort, KY 40601 Phone (502) 564-3251
Department of Military Affairs	Larry Burnette, Assistant Director Division of Emergency Management Department of Military Affairs Boone National Guard Center 100 Minuteman Parkway, EOC Building Frankfort, KY 40601 Phone (502) 607-1631

**COMMONWEALTH OF KENTUCKY  
APPENDIX 2  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of State Organization Contacts (Continued)

<b>State Organization</b>	<b>Contact</b>
Personnel Cabinet	Carl Felix, Executive Director Office of Personnel Administration Personnel Cabinet 201 Fair Oaks Lane Frankfort, KY 40602 Phone 564-2428 ext. 4114
Council on Postsecondary Education	Diann Donaldson Associate-Administrative Services Council on Postsecondary Education 1024 Capital Center Drive, Suite 320 Frankfort, KY 40601 Phone (502) 573-1555
Revenue Cabinet	Annie Hill-Pointer, Internal Auditor Office of the Secretary Kentucky Revenue Cabinet 200 Fair Oaks Lane Frankfort, KY 40601 Phone (502) 564-1553
Transportation Cabinet	Debra Gabbard, Acting Commissioner Department of Fiscal Management Transportation Cabinet 200 Mero Street Frankfort, KY 40601 Phone (502) 564-4890
Office of the Kentucky State Treasurer	Dr. Eugene Harrell, Director Disbursements Office of the Kentucky State Treasurer Capitol Annex, Room 183 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-4722

**COMMONWEALTH OF KENTUCKY  
APPENDIX 2  
FOR THE YEAR ENDED JUNE 30, 2003  
(CONTINUED)**

List Of State Organization Contacts (Continued)

<b>State Organization</b>	<b>Contact</b>
Cabinet for Workforce Development	Tommy Goins, Branch Manager Division of Fiscal Services Cabinet of Workforce Development 500 Mero Street 9th Floor Frankfort, KY 40601 Phone (502) 564-3300